



Newfoundland and Labrador

**REPORT OF THE AUDITOR GENERAL**  
**(Summary)**

**To the House of Assembly**

**for the Year Ended**  
**31 March 1999**





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## **Preface**

This document is presented as a summary of the *Report of the Auditor General to the House of Assembly on Reviews of Departments and Crown Agencies for the Year Ended 31 March 1999*. That Report contains approximately 500 pages of conclusions, commentary, recommendations and auditees' comments. When readers identify a topic of interest, we encourage them to read the relevant section in the Report. This document contains information on the items reported in Chapters 1 through 4 and are numbered to coincide with the Report.

## **Introduction**

The *Report of the Auditor General to the House of Assembly on Reviews of Departments and Crown Agencies for the Year Ended 31 March 1999* was prepared in compliance with Section 12 of the *Auditor General Act*. Section 12 requires that the Report outline significant matters noted during the course of examining the accounts of the Province, agencies of the Crown and other entities which, in our opinion, should be brought to the attention of the House of Assembly.

Comments on the audit of the financial statements of the Province are contained in a separate report entitled *Report of the Auditor General to the House of Assembly on the Audit of the Financial Statements of the Province for the Year Ended 31 March 1999*. Therefore, along with this Summary, two reports are tabled before the House of Assembly.

## **Chapter 1**

### **Auditor General's Overview**

This chapter provides an introduction to the *Report of the Auditor General to the House of Assembly on Reviews of Departments and Crown Agencies for the Year Ended 31 March 1999*.

## **Chapter 2**

### **2.1 Framework of Accountability**

While I am pleased to see that some action has been taken, I am concerned that Government has not introduced legislation designed to hold its departments, agencies of the Crown and the University accountable to the House of Assembly for their performance and use of public resources. The Bill which is presently before the House of Assembly is designed to hold only those entities which are defined as public bodies (ie. hospital boards, school boards, and regional health and community services boards) accountable for their operations, and then only if the minister requests. However, I now understand that Government has decided not to proceed with enactment of this legislation.

My review of the Hansard of the House of Assembly has disclosed that of the \$1.905 billion paid to 63 Crown entities for government operating grants for the 1997-98 year, the House of Assembly received reports on only 5 entities which had received \$163.5 million.

While Government has made some progress toward the development and design of a framework of accountability, no annual reports have been provided to the House of Assembly by Government or its departments. There is no legislation requiring Government, its departments, agencies of the Crown and the University to be accountable to the House of Assembly for their operations and use of public resources. On behalf of the taxpayers of the Province, the House of Assembly approves the allocation of resources to Government, its departments, agencies of the Crown and the University. True accountability would require that these entities, in turn, report back to the House of Assembly on their use of the resources granted. If these entities do not provide any information on their use of the resources granted to them, or if they provide information only to Government, then we cannot say that a true system of accountability exists.

Government should complete its work in establishing a framework of accountability. This framework should apply to all departments, agencies of the Crown and Memorial University of Newfoundland. If this framework is to be successful it is imperative that it be approved by the House of Assembly and enacted in legislation and that it specifically require the tabling of annual reports in the House of Assembly.

### **Chapter 3**

#### **3.1 Monitoring Agencies of the Crown**

As at 31 March 1999 there were approximately 152 (1998 - 156) Crown agencies in the Province. Of these, 83 (1998 - 85) were required to prepare annual financial statements while 69 (1998 - 71) were considered non-financial and did not prepare financial statements. Any expenditures related to the operation of these 69 entities are included with those of the government department responsible for the entity and are audited annually as part of our audit of the public accounts of the Province.

Of the 83 entities required to prepare annual financial statements, 30 (1998 - 29) were audited by our Office while 52 (1998 - 56) were audited by private sector auditors and one has not yet appointed auditors.

Most of these entities do not have any requirement to report to the House of Assembly on the discharge of their responsibilities. A major role of this Office is to monitor these entities in order to provide some accountability to the House of Assembly. Section 14 of the *Auditor General Act* requires all private sector auditing firms to submit to our Office a copy of the audited financial statements and any management letters for all Crown agencies which they audit. These financial statements and management letters along with our Office's audits of Crown agencies provide the basis for our monitoring of all Crown agencies.

### **3.2 Monitoring Expenditures of the Consolidated Revenue Fund**

As part of our audit of the financial statements of the Consolidated Revenue Fund (CRF), we perform tests and reviews of the expenditures made by the various departments.

In addition to our financial statement audit work, during the past year, we obtained expenditure information from Government's accounting system relating to all expenditures of the Consolidated Revenue Fund. We performed a general review and analysis of amounts paid relating to: grants and subsidies; property, furnishings and equipment; purchased services; professional services; allowances and assistance; and transportation and communications. Details of the expenditure of each of these categories are presented in Part 3.2 of the *Report of the Auditor General to the House of Assembly for the year ended 31 March 1999*.

### **3.3 The Canada-Newfoundland Economic Renewal Agreement**

The Canada-Newfoundland Economic Renewal Agreement was signed on 20 June 1996 to increase opportunities for economic development in Newfoundland, and specifically to enhance growth of earned incomes and employment opportunities in the Province. The Agreement covers the period 1 April 1996 to 31 March 2001 and provides funding of \$100 million, cost shared between the Federal Government (\$80 million) and the Provincial Government (\$20 million). The Agreement is comprehensive and specifically defines what is required to implement, monitor and manage the Agreement.

Our review indicated that from 1996 to 1998 there has been a steady improvement of the implementation, monitoring and management of the Agreement programs and projects. Further improvements are required and we were informed that further improvements are planned.



Our review identified two significant weaknesses which should be addressed:

- Under the Agreement, the Management Committee has the right to examine and audit the records of projects managed by third party individuals and organizations who have received funding under the Agreement. As of March 1999, these third party individuals and organizations have received \$51 million in project funding. However, no inspection or audit of these records and supporting invoices has been carried out to date. As a result, Government cannot demonstrate that all expenditures made by third parties under the Agreement were eligible for funding under this Agreement.
- Although the Management Committee established an Evaluation Framework as required under the Agreement and some useful information is being provided through this framework, adequate performance information necessary to evaluate the programs is not being provided by all of the implementing departments. In addition, since key performance targets were not included in the third party contracts there is no formal requirement for these third parties to provide this information. As a result, it will not be possible for the Management Committee to evaluate whether the objectives of the Agreement are being achieved.

### **3.4 Special Warrants**

The common parliamentary means of providing spending authority to government for its operations is through the annual passing of supply acts. This involves having the Members of the House of Assembly vote on the government's funding requests before the spending authority is provided. Approval by a majority of the Members of the House of Assembly is needed to pass an act.

Through the use of a "special warrant", Government can, without the prior approval of the Members of the House of Assembly, spend public money. Section 28 of the *Financial Administration Act* outlines two instances where a special warrant can be approved and additional funding can be provided to government.

There were 14 special warrants totalling \$136.1 million issued in the 1998-99 fiscal year, of which \$123.8 million were issued in March 1999. It is my opinion that \$95 million of the \$136.1 million of the special warrants issued in 1998-99 did not meet the requirements of the *Financial Administration Act* in that they were not urgently required and therefore should not have been issued. If these special warrants had not been issued, and in my opinion they should not have been, Government would have reported a cash surplus of \$105.1 million compared to the \$10.1 million that was actually reported.

### **3.5 Cellular Phones in Government**

Since the use of cellular phones is increasing, government should ensure adequate systems and procedures are in place.

Many Government departments do not have adequate control over the acquisition and administration of cellular phones, and not all departments have developed procedures to verify receipt of cellular service and approve invoices for payment. I am recommending that Government establish a government-wide policy to control the acquisition and administration of cellular phones.

### **3.6 Accounts and Loans Receivable in Government**

As I have indicated in previous reports to the House of Assembly, Government's systems for recording, reporting and controlling accounts receivable do not always provide timely and accurate information to users. As a result, Government does not know how much money is owed to it at any given point in time. The general exception is the amount owed as of the 31 March of each year which is determined subsequent to year end in order

to prepare the financial statements of the Province. Government anticipates that this problem will be addressed with the implementation of its new accounting system. Government introduced the accounts receivable function of its new accounting system in May 1999 and between May and October 1999 the accounts receivable function was implemented in 12 of the 15 departments.

Our review of Government departments indicates that a significant portion of their accounts receivable are in arrears and that their cash management program, which includes the collection of these accounts, is not adequate.

### **3.7 Human Resource Management Information Systems**

In 1987 Government recognized the need to more effectively manage its human resources and established a Steering Committee to develop a comprehensive computerized Human Resource Management Information System. In 1990 it was determined that a new system would cost approximately \$2.1 million and would be completed by March 1993. There were 17 functional areas that were identified as necessary to address in order to have the required system. As at 31 March 1995, Government had spent approximately \$4.3 million and no further significant costs have been incurred. At the time of our review, Government had only developed or partially developed 5 of the 17 functional areas and made enhancements to 4 functional areas. Government still does not have an adequate Human Resource Management Information System.

### **3.8 A Review of the Financial Management System**

In November 1998, Government completed the replacement of many of its key financial systems with a new integrated Financial Management System. The acquisition and implementation of the Financial Management System was one of the most significant information technology projects

undertaken by Government, involving over 15 departments and 500 users at 31 different locations. Our review indicated that the system was implemented within time and within budget.

### **3.9 Repayment of Severance and Redundancy Pay**

Government has undertaken a number of initiatives in recent years to decrease the size of the public service.

During 1996-97, 1997-98 and 1998-99, Government and its Crown agencies paid a total of \$67.5 million in ex-gratia and other payments. A significant portion of the \$67.5 million was redundancy and severance paid to displaced employees of Government departments, school boards, health care boards and other Crown agencies.

Section 17 of the *Financial Administration Act* indicates that the Minister of Finance may, subject to the approval of the Lieutenant-Governor in Council and another Act, negotiate and accept a settlement of a debt. Treasury Board Secretariat did not have the approval of the Lieutenant-Governor in Council as required by the *Financial Administration Act* when it issued its Directive stating that employees who are required to repay redundancy and/or severance benefits have the option of making lump sum repayments or negotiating a repayment schedule acceptable to their department based on their ability to pay and the salary earned in their new position. As a result, Government is in contravention of the *Financial Administration Act*.

Government's policy is unclear as to who is responsible for ensuring amounts owing for severance and redundancy pay are actually collected by Government. Furthermore, Government has not carried out any reviews to ensure employees who received severance and/or redundancy payments, and who were subsequently rehired by Government departments, Crown corporations, and other Government agencies, repay amounts owing in accordance with Government policy.

Although Minute of Council 94-520 indicates that compensation practices of Government are applicable to Crown corporations and other Government agencies, Government's current policy is silent on the issue of rehiring in these entities. Government's current policy does not address the repaying of severance and redundancy pay if an employee of one Government entity obtains employment with another Government entity.

Of 24 employees selected for review to determine compliance with the *Financial Administration Act* and Government's Re-employment Priority Policy, we found a number of instances of non-compliance.

I am recommending that Government comply with the *Financial Administration Act* and determine whether employees who receive severance pay and/or redundancy pay and were subsequently rehired, have repaid the amounts owed.

### **3.10 Strategic Enterprise Development Fund**

The Strategic Enterprise Development Fund is administered by the Department of Development and Rural Renewal. The Fund provides capital financing to assist the start up and growth of small and medium sized businesses which have activities consistent with strategic sectoral opportunities identified as zonal or provincial priorities and whose funding needs cannot be met through other sources. Capital financing may take the form of loan advances, equity advances, loan guarantees, company development grants or conditional forgivable loans.

The Province provided \$18,100,000 to the Fund in 1996-97, \$7,000,000 in 1997-98 and \$8,975,000 in 1998-99. These funds were then transferred to Enterprise Newfoundland and Labrador (ENL) to provide capital financing to various individuals and entities.

Our review indicated the following:

- Reporting on the performance of the small business loan program is inadequate. There are no reports on the actual

number of jobs created or what economic benefit has resulted from the loan program. Each year approximately \$7.0 million is invested in this program without adequate structures in place to determine if the program is achieving its intended purpose and without any reports, other than audited financial statements, to the House of Assembly on what has been achieved. In June 1999 the Department prepared a report on approvals and employment by industry sector; however, this is an internal report and is not required on a regular basis. It was not provided to the House of Assembly.

- Assessment of loan proposals was not always adequate as significant pieces of information were not included in the assessment. Our review identified concerns with 7 of the 42 files reviewed regarding the adequacy of the assessment of the proposal.
- Loans were made to companies that had existing loans in arrears or when there were indications that management was not acting in good faith. Our review identified concerns with 7 of 42 files reviewed regarding the future viability of the proposal.
- Adequate security was not always obtained prior to the loan disbursement and funds were disbursed prior to conditions for the loan being met. Our review identified concerns with 4 of 42 files reviewed regarding the adequacy of security.
- Once the loans are issued there is inadequate follow up to ensure the conditions for the loan continue to be met. Required financial information is not always submitted to the regional offices and there are very few personal visits or contact with the loan clients documented in the files. Without these visits the Department cannot ensure the loan security is still in place and the business is operating in accordance with the loan agreement.

- Only 25% of ENL's total loan and equity portfolio of \$78.2 million is estimated to be recoverable. The remaining 75% is an estimate of the uncollectible accounts and has been provided for in the allowance for doubtful accounts. This estimate is a matter of judgement and the actual collections may be more or less.

### **3.11 Strategic Enterprise Development Special Reserve Fund**

The Department of Development and Rural Renewal administers the Strategic Enterprise Development Fund and through this fund provides assistance to small and medium size businesses. Over 90% of the \$11,975,000 in the Special Reserve Fund was provided to three companies. There are stated objectives for the fund and standard procedures to be followed in assessing, approving and monitoring assistance provided to businesses through this fund. Our review disclosed that these procedures were not followed for the three projects that we reviewed under the Special Reserve Fund of \$11,975,000. For example:

- Although the Department of Development and Rural Renewal, through Enterprise Newfoundland and Labrador Corporation, was responsible for the disbursement of the funds, it had very little to do with the assessment, approval and monitoring of the three projects that we reviewed under the reserve fund. The Department of Industry, Trade and Technology was responsible for the call centre projects and the subsequent monitoring of these projects, while the Department of Finance was responsible for Newfoundland Bonding & Composites Limited. It was evident from our review that these projects were pre-approved before the Board of ENL or the Department became involved.
- Our review of three approved projects funded through the reserve fund indicated that they were not subject to the policies and procedures as established for other loan and equity investments. Thorough assessments were not performed, verification of business plan assertions was limited and monitoring was inadequate.

### **3.12 The Enterprise Network Inc.**

The Enterprise Network Inc. is a Crown corporation which was established to make commercial, technical, and industrial information equally accessible to individuals and organizations in urban, rural and remote regions of the Province. The Corporation commenced operations in 1991 and closed its head office and five telecentres in 1997. Over the seven year period, the Corporation had spent approximately \$1.9 million on capital assets. When the Corporation closed in 1997, it decided to distribute its capital assets to various government departments, Crown agencies and community groups. Our review indicated the following:

- 1) The Corporation did not maintain adequate records on its capital assets and as a result, the Corporation could not provide us with a listing of assets that should have been on hand when it ceased operations in October 1997.
- 2) As a result of the inadequate records on capital assets, the Corporation could not indicate exactly what was the final disposition of its capital assets totalling \$1.9 million.
- 3) Although there were listings prepared for assets transferred to government departments and Crown agencies, the listings were deficient in that there was no cost information provided which would relate these assets back to the total assets of \$1.9 million.
- 4) The Corporation did not maintain listings of the individual assets and their costs which were distributed to each of the community groups. After our enquiry, the Corporation contacted some of the community groups and obtained asset listings. However, these listings were not independently prepared by the community groups and appeared to be photocopies of listings prepared by the Corporation at various dates prior to or during October 1997. Such listings included references to assets as "missing" or being located at employees' homes.



### **3.13 Provincial Post Secondary Awards Program**

Government, in 1998 announced a \$4,000,000 provincial post secondary awards program over a two year period, intended to provide awards to post secondary students based on academic merit and financial needs. This Program is intended to provide a bridge to the new \$2.5 billion Canada Millennium Scholarship Program which commences in 2000. The Provincial Post Secondary Awards Board was established in May 1998 to formulate awards criteria and general administrative procedures regarding the program. Awards were available to students who obtained a student loan from the Department of Education which was insufficient to meet all of their assessed financial need.

As at 31 March 1999, 1,601 students received awards totalling approximately \$1.3 million.

The Department has no documented policies and procedures with respect to the delivery of the provincial post secondary awards program and there is no evidence that the established eligibility criteria were ever approved by the Provincial Post Secondary Awards Board.

There are weaknesses in the process which the Department is following to determine the amount a student is entitled to receive. We found numerous and significant errors in amounts awarded to students as a result of the timing of the award calculation.

Significant issues raised at the Provincial Post Secondary Awards Board meetings have not been addressed by the Board in a timely manner. For example, the time the reports should be produced to determine the amount of an award, the establishment of an appeals process, and the establishment of institutional sub-committees have yet to be resolved.

### **3.14 Deferred Bursaries**

Prior to the introduction of the Newfoundland Student Loan Program in 1994-95, the Province administered a Deferred

Bursary Program which was intended to offset student debt which was borrowed under the Canada Student Loan Program. This program provided students, who qualified, with bursaries which were deferred until the student consolidated their Canada Student Loan at the bank for purposes of repayment. The bursaries are paid out when the student begins to repay their Canada Student Loan. As at 31 March 1999, there were approximately 7,900 students still entitled to receive approximately \$6.0 million in deferred bursaries which were approved prior to July 1994.

We found that the Department does not have procedures in place to ensure that all students are paid the \$6.0 million in bursaries they are eligible to receive. A significant number of annual notifications mailed to students in 1998 advising them of their outstanding deferred bursaries, were returned to the Department marked undeliverable. Currently, the Department has no plans to address the undelivered notifications or the large number of deferred bursaries still outstanding.

### **3.15 Loan Remission Program**

The Department of Education administers a Loan Remission Program through its Student Aid Division. The Loan Remission Program was announced by the Province in 1994-95 coinciding with the introduction of the Newfoundland Student Loan Program in 1995 and the earlier termination of the Deferred Bursary Program (see Item 3.14 of this Report) in 1993. However, students were not eligible to commence applying for a loan remission until September 1997. The Loan Remission Program is intended to encourage students to pursue their post-secondary education in Newfoundland and to complete their program of study in a timely fashion by offering a debt forgiveness incentive to students who borrow.

Loan Remissions are provided to borrowers who qualify in accordance with established loan remission criteria. The success of this program depends largely on the Department's efforts to inform students when they begin and continue through their program of study as to the eligibility criteria they must meet in

order to qualify for a loan remission at the end of their program of study.

As of 31 March 1999, the Department approved 661 loan remissions totalling approximately \$3.5 million. Of the \$3.5 million, \$900,000 was paid in 1997-98 and \$2.6 million was paid in 1998-99.

Although the Loan Remission Program was announced by Government in 1994, the eligibility criteria were not finalized and conveyed to students until the 1997-98 academic year. As a result, students enrolled in programs prior to the 1997-98 academic year may have been unaware of the criteria they would be required to meet in order to qualify for a loan remission on completion of their program of study. It is unfair to require students to comply with criteria that they were not aware of at the time of their studies and which had yet to be finalized. It is possible that some students who did not meet the graduation period eligibility criterion would have made a concerted effort to complete their academic programs within the appropriate time frames if they had known this at the time they were pursuing their studies.

The Department was not applying its criterion of requiring students to submit their loan remission applications within 90 days of completing their studies. As a result, we found instances where, because the Department relaxed its loan remission application deadline criterion of 90 days, it was unable to process all loan remission applications in a timely manner and forward them to CIBC within the required 180 day time frame necessary to avoid being charged the 5% risk premium.

It is possible that students who did not meet the 90 day application deadline would have applied if they had known that the Department had relaxed the deadline criterion of 90 days.

We found instances where the Department failed to process loan remission applications in accordance with established guidelines. Of the 38 loan remission applications reviewed, 9 did not meet all of the established guidelines. In one case, a student was

awarded a loan remission of \$5,225 although the student did not meet the established criteria.

### **3.16 Student Loan Program**

In 1994-95, the Department of Education and Training commenced the delivery of the Newfoundland Student Loan program through its Student Aid Division. The Newfoundland Student Loan Program is delivered along with the Canada Student Loan Program. While both loan programs are separate from one another, there is sufficient harmony in the loan programs to permit delivery as one program. Student loans are issued at 60% and 40% under the federal and provincial programs respectively and the costs of servicing are shared, for the most part, on the same basis.

As of 31 March 1999 there was \$223 million in issued and outstanding student loans of which \$87 million relates to loans currently on repayment by students who have completed their studies. Of the \$87 million in student loans which is currently subject to repayment, \$29.4 million or 34% is in arrears greater than 30 days. This is similar to 31 March 1998 when \$18.5 million or 35% of the \$50.3 million in student loans under repayment were in arrears greater than 30 days.

Currently, there is no written agreement between the Federal government and the Province governing the delivery of the Canada and Newfoundland Student Loan Program by the Province.

The current *Student Assistance Act* was enacted in 1996 and does not adequately reflect the changes which occurred in 1994-95 when the Province moved from a grants based program to a loans based program. In addition, in 1996 the *Student Allowances Regulations*, which related to student programs that are no longer available, were eliminated. As a result, the Newfoundland Students Loan Program is currently being administered without the appropriate legislative authority.

The Department does not have its own policy manual for the administration and delivery of its student loan program. The Department maintains that it is administering its student loan program, for the most part, in accordance with policies issued by the Federal government for its Canada Student Loan Program. However, our review indicated many instances of non-compliance with these policies, the details of which are included in my Annual Report.

The appeals process is currently coordinated through an Appeals Officer and an Appeals Board. There are weaknesses in the student loan appeals process and these are included in detail in my Annual Report.

In order for students to be eligible for student loans, the institution they are attending must be "designated" for purposes of student loans under the *Student Assistance Act*. The *Student Assistance Act* does not provide any guidance as to how an educational institution should be designated for purposes of student loans since there are no regulations established for this purpose under the *Act*, even though there is provision in the *Act* to do so. The Department maintains that it has been designating private educational institutions for purposes of student loans if they meet private training institution licencing requirements under the *Private Training Institutions Act*. Effective 1 January 1999, for purposes of student loans, the *Private Training Institutions Regulations* were amended to state that "*Notwithstanding the Student Assistance Act or regulations, a private training institution shall not be designated as an institution which offers courses for which student assistance is available unless it has been in continuous operation as a registered private training institution for one year and has graduated one class of students*".

There are no approved guidelines or procedures in place to ensure that the Department can effectively monitor student loan default rates at designated educational institutions. Designated educational institutions with unacceptable student loan default rates may indicate that these institutions are experiencing program and/or operational problems. Our review indicated

that for 1997-98, 23 of 54 educational institutions in this province had student loan default rates in excess of 30%. We could not determine if these default rates were acceptable to the Department. Draft Canada Student Loan Designation Guidelines as prepared by the Federal Government for discussion purposes, for example, suggest that for 1997-98, institutions with default rates greater than 30% and less than 55% should be placed on "probation".

In October 1998, an internal departmental committee released its report on "Designation for Student Aid Purposes" to address weaknesses in the Provincial designation process. The Department has indicated that it intends to forward its draft designation policy to educational institutions for their input in the near future. We are concerned that a report dated October 1998 on such a significant issue has yet to be implemented in light of the significant increase in the number of students attending private educational institutions.

The Department has not reviewed error reports related to billings from the bank for interest subsidy, interest relief and risk premiums since December 1996. Our review of the exception report dated 31 October 1998 indicated that the exceptions total approximately \$840,000. These exceptions could represent amounts paid by the Department in error.

The Department has honoured guarantees on defaulted loans totalling \$1.9 million. It is now the Department's responsibility, and not the bank's, to collect these loans. The Department does not have any policies on the collection of these loans. Although some former students offered to repay their loans, the Department would not accept payments because it did not have a collection process in place.

The Province is currently negotiating an extension to the lender agreement in place with the bank with respect to student loans that expired on 31 July 1999. As a result of increasing student loan default rates and the Department's failure to adequately monitor student loan default rates, the Province is expecting the 5% risk premium it is currently paying on Class B student loans

to increase to between 10% and 15%. This will result in risk premium costs increasing from \$2.1 million in 1998-99 to between \$4.7 million and \$6.6 million in 1999-2000.

The automated system being used to handle student telephone inquiries is not adequate. Information obtained from the Department indicated that there is an average of 2,290 calls per day made to this system and the majority of callers do not utilize its automated features, but request to speak to the operator instead. One operator cannot process all these inquiries in a timely manner.

The Switchboard at Student Aid is intended to direct callers to their appropriate destination. We found that a significant percentage of calls made to the Student Aid switchboard operator are abandoned before the switchboard operator can answer.

The Department has not established goals, objectives and performance indicators for the Newfoundland Student Loan Program. While the Student Aid Annual Report is a comprehensive and detailed document, the information provided in it cannot be utilized in monitoring performance because the Department has not established goals and objectives to compare the information against. In addition, the Department is not compiling performance information such as the length of time it takes to process an application for a student loan or the length of time it takes to process appeals.

### **3.17 Monitoring of School Boards**

In 1996 the school system in the Province was reorganized with the dissolution of 27 church run school boards and the creation of 10 new English language school boards and one French language school board. The 27 school boards continued to exist and administer the schools within their jurisdiction until their dissolution on 31 December 1996. As at 31 December 1996, there were approximately 445 schools in the Province with a total enrolment of 110,450 students. In the 1998-99 school year there were 365 schools with an enrolment of 97,400 students.

In the reorganization process, the Province decided to eliminate the existing debt of the 27 school boards as at 30 June 1996. As a result, in March of 1997, the Province paid the 10 district boards \$24.2 million to retire existing long-term debt and operating debt as of 30 June 1996. However, this did not completely eliminate the deficits as the boards operated from July to December 1996 and additional deficits arose. In March of 1999, the Province paid an additional \$1.2 million to five school boards to cover these additional operating deficits.

Our review of the financial position of the 11 school boards did not identify any significant problems with the exception of School Board #7, Burin Peninsula School Board, which had an accumulated operating deficit of \$1.5 million as at 30 June 1999 which is comprised of a \$700,000 deficit in 1996-97, a \$400,000 deficit in 1997-98 and a \$400,000 deficit in 1998-99. In addition, this Board was unable to provide us with audited financial statements for the year ended 30 June 1999 at the time of our review in November 1999.

Using 1995-96 as the base year which was the last full year that the former 27 school boards operated, school board provincial revenues have declined by \$27.0 million, including \$18.5 million in teaching services grants and \$8.5 million in other revenues. The total revenue per pupil increased by 7% from \$4,796 in 1995-96 to \$5,137 in 1998-99.

Using 1995-96 again as the base year, school board expenditures declined by \$25.3 million, comprising \$17.8 million in instructional, \$5.3 million in administration, and \$2.2 million (net) in other expenditures. Expenditure on instruction per pupil increased 9% from \$3,841 in 1995-96 to \$4,173 in 1998-99.

### **3.18 A Review of the Multi-Materials Stewardship Board**

On 15 January 1997 Government implemented a Beverage Container Control Program in which consumers pay a deposit on beverage containers and receive a refund upon returning the containers to one of the 37 established depots in the Province. In addition to paying refunds to consumers, deposits, along with



proceeds from the sale of collected containers, are used to support the operating costs of the Beverage Container Control Program. All excess monies are to be paid into the Newfoundland and Labrador Waste Management Trust Fund to be used to provide funds for Government-approved waste management initiatives.

In June 1996, Government established the Multi-Materials Stewardship Board to manage the Beverage Container Control Program and the Waste Management Trust Fund. In 1997, the Multi-Materials Stewardship Board entered into an agreement with Newfoundland Beverage Recovery Inc. to operate, maintain and manage the Beverage Container Control Program on behalf of the Multi-Materials Stewardship Board. Newfoundland Beverage Recovery Inc. is a not-for-profit corporation established by the beverage industry for the purpose of carrying out the responsibilities of this Agreement.

Under this Agreement, distributors of beverage containers remit the deposits to Newfoundland Beverage Recovery Inc.. The Newfoundland Beverage Recovery Inc. holds all excess monies until directed by Government to pay the funds into the Waste Management Trust Fund. As of 31 March 1999, net assets of Newfoundland Beverage Recovery Inc. totalled approximately \$7.0 million. In July 1999, Cabinet directed that \$3.0 million of the \$7.0 million at Newfoundland Beverage Recovery Inc. be transferred to the Waste Management Trust Fund to be used for the purpose of supporting community-based environmental initiatives, such as community clean-ups, recycling and environmental education programs.

Our review indicated that the Multi-Materials Stewardship Board is adequately monitoring the management of the Beverage Container Control Program. However, several significant issues were identified during our review. For example:

- In 1996, Government established target recovery rates for beverage containers sold at 50% for 1997, 60% for 1998, 70% for 1999, and 80% for 2000. Our review in November 1999 found that the target recovery rate has

stagnated at approximately 50%. A consultant has recently been contracted to review the effectiveness of the Beverage Container Control Program.

- Under the Agreement between the Multi-Materials Stewardship Board and Newfoundland Beverage Recovery Inc., the Board has the right to inspect and audit all the records of the Newfoundland Beverage Recovery Inc. The Board has not exercised its right to inspect and audit those records as they relate to expenditures. This is significant since annual expenditures are approximately \$8.0 million.
- The Newfoundland Beverage Recovery Inc. is not submitting an annual budget and work plan for program activities for approval of the Board as required under the Agreement between the Newfoundland Beverage Recovery Inc. and the Board.

### **3.19 Newfoundland Government Sinking Fund**

Sinking funds are a pool of cash and investments accumulated by the Government during the life of a debenture, which will be used to pay off that debenture when it matures. Some sinking funds are mandatory because of a requirement outlined in the debenture issue while others are voluntary. The Province has been maintaining sinking funds for many years.

The total amount of cash and investments in the sinking funds varies each year as Government uses cash and investments to retire some debentures while contributing additional cash to sinking funds to repay other debentures.

As at 31 March 1999, the Province had accumulated \$1.02 billion in its sinking funds which will be used to retire the \$5.6 billion in debenture debt. Of the \$1.02 billion, \$571 million are mandatory while \$449 million are voluntary. The Province maintains these voluntary sinking funds even though there is no legal requirement to do so. Government has still not conducted any cost-benefit or other analysis to determine whether it is making optimal use of its cash resources

by maintaining \$449 million in voluntary sinking funds. This raises the issue of whether this is the most efficient use of cash given the Province's borrowing requirements.

### **3.20 Sale of the Nain Banker**

In my 1997 Annual Report to the House of Assembly, I reported on the four middle distance fishing vessels which had been constructed by the Marystown Shipyard Limited in the 1980's and which were operated by four corporations created solely for that purpose.

In 1995, three of the four middle distance fishing vessels were sold. The Belle Isle Banker and the Makkovik Banker were sold to Norwegian interests and the Funk Island Banker was sold to local interests. The fourth remaining vessel, the Nain Banker, was leased to the Fisheries and Marine Institute of the Memorial University of Newfoundland.

In 1997, the Nain Banker was leased to the Torngat Fish Producers Co-operative Society. In 1999, the Nain Banker was sold to the Labrador Fishermen's Union Shrimp Company Limited.

As at 31 March 1999, the Province's involvement with the four middle distance fishing vessels has cost approximately \$30.7 million.

In March 1998, there was a public proposal call for the purchase and/or lease of the Nain Banker. However, in evaluating the proposals, the Board used criteria which was not disclosed in the proposal call and gave preference to bidders who met the undisclosed criteria. Specifically no preference criteria as to where the catch would be landed or where the successful bidder would be based were included as part of the information package accompanying the 1998 request for proposals; however, such criteria were used in awarding the lease.

Three proposals received in 1998, one at \$1.5 million and two at \$1.1 million, resulting from a call for proposals for the sale of the Nain Banker, were eliminated based in part upon financial constraints associated with a required buy-out of the lease obligation. The vessel was sold in March 1999 to another company for \$1 million, only after the referenced lease buy-out had been completed. There was no indication that the three bidders with bids higher than the one accepted were contacted.

### **3.21 Belleoram Scallop Hatchery**

In 1995, Cabinet approved the redevelopment of the former provincial fish plant in Belleoram into a scallop hatchery. This initiative was based on a need for scallop spat (seed) to promote scallop development in the Province, as recommended by the Department. The intent, as stated in the Cabinet approval, was to establish the hatchery but to privatize it as soon as possible. This has not been done to date.

At the time of our review in relation to this year's report item, the Department indicated that Cabinet had been updated on the situation with the hatchery and that support had been expressed to attract a private sector company to buy or lease the facility.

In our 1998 report item, it was indicated that as at 31 March 1998, a total of \$1.5 million had been spent in capital and operating costs relating to the hatchery. Essentially all of this funding was provided either by Government directly or through Federal/Provincial agreements. The amount of investment had increased to \$1.8 million as at 31 March 1999.

A review of information maintained at the Department at the time of our 1998 review indicated that net sales totalled \$5,000 and that production targets were expected to be 7.5 million spat for 1995, the first year of operation and 15 million spat in 1996, the second year. Actual production was approximately 3 million spat in 1995 and was similarly low for 1996. As part of our update review, we determined that production had increased to 5 million spat for 1998; however, this is still less than the original estimated production capacity of 15 million.

The Department also provided that while production of seed for 1999 was expected to total approximately 5 million, the provincial seed requirement for the next two to three years is likely to be 2 to 3 million. In addition, at a 5 million production level, and at an average sales price of \$0.035 per seed proposed by the Department, annual gross revenue would be only \$175,000. The annual operating budget for the hatchery is higher than this amount, which would likely result in deficits.

In July 1999, the Department prepared a Divestiture Information Package relating to the proposed sale of the hatchery. The Department indicated that it was decided later not to release the package.

In the same month a report was prepared by the Department's Aquaculture Branch. In the report, it was proposed to continue financial support for the 1999/2000 year and to develop a plan to privatize the Belleoram Hatchery by April 2000.

### **3.22 Sale of Assets**

The Department of Fisheries and Aquaculture has a primary mandate to promote the ongoing development of marine fisheries and the aquaculture industry in the Province. Over the years, the Department has made a significant investment in infrastructure in relation to this mandate, through the construction or acquisition of various fisheries related facilities. In recent years, the Department has continued its divestiture effort relating to many of these facilities.

Information provided by the Department indicates that in excess of three hundred major assets have been subject to the divestiture process, with in excess of one hundred assets remaining under Government ownership. Assets subject to divestiture included marine service centres, fish plants, middle distance fishing vessels, community stages, bait sheds and slipways. Assets such as community stages, bait sheds and slipways were in most instances transferred for nominal amounts to local community groups. Two major categories of assets which sold for amounts other than nominal value are marine service centres and fish

plants.

### **Marine Service Centres**

Specific direction and terms of reference for the divestiture of Marine Service Centres were established by the Lieutenant-Governor in Council in January 1997. The divestiture process provided that the incumbent lessees were to be given the option of making an offer to the Department of Fisheries and Aquaculture for the purchase of the respective Marine Service Centre.

Four of the five Marine Service Centres reviewed were sold to incumbent lessees at negotiated prices. The fifth Marine Service Centre was sold as a result of a public request for proposals. In the five cases reviewed, the Department of Fisheries and Aquaculture generally complied with the direction provided by the Lieutenant-Governor in Council. In all cases, the sales price was significantly less than the appraised values and the capital cost as recorded by the Department.

For the four MSCs sold to the incumbent lessees at negotiated prices, departmental officials indicated that an acceptable price was based upon the judgment of the Government's Divestiture Committee and the particular circumstances surrounding the facility. If Government had called public proposals with the condition that the lessees had the first right of refusal, an acceptable price could have been established through a public proposal call which could have been used as a minimum acceptable offer in negotiations with the current lessee.

### **Fish Plants**

Specific direction and terms of reference for the divestiture of the fish plants were established by the Lieutenant-Governor in Council in May 1990. The divestiture process provided that the incumbent lessees were to be given the option of making an offer to the Department of Fisheries and Aquaculture for the purchase of the respective fish plants. If a negotiated price with the lessees could not be reached, the Department of Fisheries and

Aquaculture was to call a public proposal for the sale of the fish plant. The five fish plants reviewed were vacant; therefore, there was a requirement for a public proposal call. Four of the five fish plants reviewed were sold as a result of a public proposal call and accordingly complied with the direction of the Lieutenant-Governor in Council. Amounts received by the Department of Fisheries and Aquaculture for the five fish plants were significantly lower than appraised values.

### **The Lawn Fish Plant**

The fish plant in Lawn was sold to an unsolicited bidder without the benefit of a public proposal call. As a result, this sale did not comply with the direction of the Lieutenant-Governor in Council which required a public proposal call. In addition, a review of departmental files disclosed that six other unsolicited expressions of interest had been received prior to the sale of the Lawn fish plant.

Authorization by the Lieutenant-Governor in Council for the sale of the Lawn fish plant included a requirement that the Department of Fisheries and Aquaculture receive a written commitment from the buyer regarding capital investment and employment levels. A letter was received from the purchaser indicating plans for investment of \$300,000 over five years and disclosing the current average weekly employment level; however, sale documents did not include any commitment as a condition of the sale. An official of the Department indicated that there has been no follow-up to determine the amount of capital investment to date or the recent employment history of the fish plant at Lawn.

### **3.23 Aquaculture Program**

In my 1998 Annual Report I commented on the issuance of a loan guarantee to an aquaculture licensee. Government's involvement with this aquaculture licensee is estimated to have cost the Province a total of \$9.3 million in loans and loan guarantees as of 31 March 1999. Despite the infusion of \$9.3 million from Government, the licensee's financial position

has deteriorated significantly.

Of the \$9.3 million, \$2.8 million is owed to Enterprise Newfoundland and Labrador Corporation and \$6.5 million relates to a loan guarantee. Government paid \$5 million of the loan guarantee in March 1999 and expects to pay the remaining \$1.5 million in 1999-2000. It is unlikely that Government will recover any of the \$9.3 million.

Although Government initially had security in place for these loans and loan guarantees, Government relinquished some of its security in favour of other creditors in an effort to keep the company operational.

### **3.24 Legacy Nature Trust**

On 22 March 1999, Government announced in its 1999 Budget Speech the establishment of the Newfoundland and Labrador Legacy Nature Trust. The trust was to be established as a non-profit agency with a mandate to raise funds nationally and internationally to finance conservation projects in Newfoundland and Labrador. In the 1999 Budget Speech Government made a commitment to contribute \$1 million to the Trust.

On 12 March 1999, Government issued a special warrant for \$1 million indicating that these funds were urgently required for the Newfoundland and Labrador Legacy Nature Trust. On 31 March 1999, a cheque for \$1 million was issued and recorded as an expenditure in Government's fiscal year ended 31 March 1999, thus increasing Government's expenditures by \$1 million and reducing Government's cash by \$1 million.

It concerns me that Government has circumvented the *Financial Administration Act* by issuing a cheque for \$1 million on an urgent basis on the last day of the fiscal year to a Corporation which did not exist. I am also concerned that this cheque was in the possession of Government officials for 43 days before it was deposited. When it was finally deposited, it was held in a bank account used for bid deposits which accompany public tenders, a purpose entirely unrelated to the nature of the cheque.



### 3.25 Newfoundland Farm Products Corporation

Newfoundland Farm Products Corporation was established in 1963 under the *Farm Products Corporation Act*. As a Provincial Crown corporation, Newfoundland Farm Products Corporation produced a full range of chicken products which were marketed throughout the Province, the Maritimes and central Canada. Over a ten year period from 1987-88 to 1996-97, the Corporation incurred average annual operating losses of \$4.3 million.

A new Board of Directors was appointed in November 1996 and given the mandate to pursue privatization of the Corporation. In October 1997, the sale of the St. John's processing operation to Integrated Poultry Limited, a consortium of local chicken producers, was concluded. The processing operations in Corner Brook were closed by Government in April 1997.

Financial and other assistance has been provided by Government to Integrated Poultry Limited since 1997 as follows:

- In 1997, Government provided \$8.5 million in operating and capital grants to Integrated Poultry Limited.
- Under the terms of the Purchase and Sale Agreement and the subsequent Share Purchase Agreement, Integrated Poultry Limited was to pay \$2.0 million to Newfoundland Farm Products Corporation for \$1.4 million for inventory and \$.6 million for operating losses incurred when Newfoundland Farm Products Corporation was jointly managed by Government and IPL.

On 4 October 1997, \$500,000 of the \$.6 million due to Government for operating losses incurred when Newfoundland Farm Products Corporation was jointly managed by Government and IPL was repaid. As at March 1999, the remaining \$1.5 million was still owing to Government. In January 1999, Government and Newfoundland Farm Products Corporation agreed to restructure the repayment terms on the \$1.5 million note

receivable from Integrated Poultry Limited. Repayments were originally due to commence in January 1999 but have been restructured to be repaid over a 12 month period, commencing in January 2000.

- In October 1997, Government provided a \$10.0 million term loan guarantee to Integrated Poultry Limited. In December 1998, Government increased the \$10.0 million loan guarantee by \$1.5 million for a total of \$11.5 million.
- In October 1997 Government provided a working capital deficiency loan guarantee for \$1.0 million.
- In December 1998, Government also issued a new loan guarantee in the amount of \$400,000 which has since been repaid.
- In April 1999, Integrated Poultry Limited requested Newfoundland Farm Products Corporation to provide the initial financing up to \$1.7 million to purchase a grain shipment. Newfoundland Farm Products Corporation paid for this shipment by borrowing \$1.5 million from a bank as authorized by the Lieutenant-Governor in Council. This loan was guaranteed by the Province. In May 1999, Integrated Poultry Limited repaid the \$1.5 million to Newfoundland Farm Products Corporation and the related loan guarantee by the Province was canceled.
- In October 1999, IPL requested Newfoundland Farm Products Corporation to provide financing for another shipment of grain. In November 1999, the Lieutenant-Governor in Council authorized Newfoundland Farm Products Corporation to borrow up to \$1.7 million to purchase the grain shipment. This loan was guaranteed by the Province. The loan is to be repaid by 31 May 2000 from the proceeds of the sale of the grain to IPL Processing Limited and/or other customers as deemed appropriate. At the end of our review, Newfoundland Farm Products Corporation had borrowed \$1.4 million towards this grain shipment.

- In October of each year, Integrated Poultry Limited is to remit an annual loan guarantee fee, in the amount of 1% of the outstanding loan guarantee, to the Department of Finance. In March 1999, Integrated Poultry Limited did not have sufficient cash to pay the loan guarantee fees of \$110,000 which was owing from 1998 and the 1999 loan guarantee fee of \$126,000 which was to be billed in October 1999. At IPL's request, Government agreed to receive monthly payments of \$20,000 commencing 1 April 1999 until both amounts due are paid in full. Our review disclosed that monthly payments of \$20,000 were received from April 1999 to September 1999 and totalled \$120,000.

In preparing its 31 March 1999 financial statements, Government determined, in December 1999, that it will most likely have to honour its \$12.8 million loan guarantee for Integrated Poultry Limited. As a result, included in the Province's liabilities in the Consolidated Revenue Fund Financial Statements for the year ended 31 March 1999 is a provision of \$12.8 million for possible losses on the \$12.8 million loan guarantee.

During 1998-99, in order for IPL to obtain financing, Government relinquished a portion of its security on the assets of Integrated Poultry Limited.

On 15 December 1999, the bank demanded payment, by 7 January 2000, from Integrated Poultry Limited for its loans and issued a "Notice of Intention to Enforce Security". As a result, on 16 December 1999, Government paid the \$11.5 million under guarantee to the bank and for the \$1.0 million guarantee, elected to require the bank to realize upon its security and to notify the Government of the amount of any deficiency up to the \$1.0 million guarantee. On 20 December 1999, Government demanded payment of the \$11.5 million from Integrated Poultry Limited and on 21 December 1999, Government issued a "Notice of Intention to Enforce Security" to Integrated Poultry Limited.

In late December 1999, Government and the bank formed a secured Creditor Committee and on 10 January 2000, Government, the bank and Integrated Poultry Limited signed a Forbearance Agreement which will expire on 31 January 2000 unless it is extended. The purpose of this Agreement is to allow Integrated Poultry Limited the opportunity to continue its search for new equity or other investors, without being subject to further action by Government and the bank with respect to exercising their security in the interim, as well as to operate in the manner permitted by the Agreement. Under this Agreement, if Integrated Poultry Limited is unsuccessful in restructuring its debt or attracting a new investor, Integrated Poultry Limited has agreed that it will not oppose Government and the bank should they choose to realize upon their security by requesting the Courts to appoint a Receiver.

### **3.26 Management of Crown Lands**

The Department of Government Services and Lands is responsible for the management of the Province's Crown lands. Crown lands comprise approximately 95% of the Province's land mass and as such is one of the Province's most significant natural resources. The management of Crown land is assigned to the Lands Branch of the Department of Government Services and Lands. This Branch is comprised of three Divisions: Crown Lands Administration, Surveys and Mapping, and Land Management. The Branch's responsibilities include processing land applications, preventing unauthorized use of Crown land, resolving conflicts in land use and ownership, producing a map inventory of land in the Province, and developing land use policy and management plans. Our review of the Department's management of Crown land indicated the following:

- There is no comprehensive and complete land parcel identification system for all land in the Province and therefore, Government does not know the extent or boundaries of Crown lands in the Province. As a result, it is more difficult for Government to effectively manage and plan the use of Crown lands, and Government's land allocation and designation processes are more extensive

and time consuming.

- The Province does not have comprehensive land use policies to facilitate a co-ordinated approach for land use within Government. As a result, planning for land use within Government is fragmented and covers only small areas of the Province. Discussions with Departmental officials indicated that a comprehensive land plan for the entire Province is not practical due to the significant costs involved. However, it would be prudent for Government to complete comprehensive land plans for certain areas of the Province including those areas where potential for conflict over land use exists.
- The following observations were noted with respect to application processing:
  - A review of 22 selected land applications indicated that, in general, applications are being processed in accordance with legislation and Departmental policy.
  - A recent Departmental report on the Crowns Land Division recognized a number of areas that cause delays in the application process that could be improved including the process for referring applications to other Government departments and agencies and the process of referring applications from the Government Service Centres to the Regional Lands Offices.
  - Information maintained in the Department's system that tracks the progress of an application is often inaccurate. This reduces the usefulness of the information to monitor the status of applications. Discussions with staff in the Regional Offices also indicated that they do not generally review the reports available from the system to monitor applications nor do they generally monitor the status of applications.

- A sample of 30 dispositions of Crown land indicated that for the sample selected, adequate information, in the form of appraisals performed either by the Municipal Assessment Agency or by Departmental staff, was available to support the fair market value assessed on the property.
- The Land Management Division does not maintain adequate information on cottage lot developments, including the status of the lot sales and the associated costs and revenues. Accurate and complete information on status of the development and associated costs and revenues would enhance information available to Management for the monitoring of existing developments and the planning of future developments.
- Companies that have approved status under the *Economic Diversification and Growth Enterprises Act* (EDGE) have been approved to lease certain Crown land at \$1. Although Departmental officials were aware that a number of EDGE companies had leased Crown land at \$1, they could not provide us with any information regarding which EDGE companies had leased this land, what land had been leased, or what the land was being used for. The Department of Industry, Trade and Technology, who are responsible for administering the EDGE program, also could not provide us with any of this information. Thus, there has been no monitoring of the status of this land or whether these companies still have eligible EDGE status. We also noted that there is nothing in the agreements between Government and EDGE companies to address what would happen to this land if the company lost its EDGE status.

After significant effort by staff of the Department a list of EDGE companies that are leasing Crown land at \$1 was provided to us. A comparison of this list with those EDGE companies that have had their status revoked indicated that all of the companies that are leasing Crown land for \$1 still have EDGE status.

- Monitoring procedures to ensure that the lessee has adhered to the terms of the lease with respect to type of development and period to complete development, is usually limited to sending out affidavits to individuals, after five years have lapsed, which the individual completes to attest to the fact they have adhered to these terms. We also noted that some of the Regional Offices are not even sending out these affidavits. As a result, the Department cannot determine whether Crown land is being used for the purposes intended when the land was authorized for disposition.
- Although a review of a sample of leases indicated that billings were properly prepared and recorded in the accounting records, we noted that for those leases where title to the land will only be transferred to the lessee after the lease is paid off over 5 years, the Department has only recorded the current portion or 1/5 of the balance owing in the accounting records.

We noted weaknesses with respect to the collection of accounts. More specifically \$1.3 million or 48% of the accounts receivable at 31 March 1999 of \$2.7 million were in excess of one year overdue. The Department does not monitor these accounts nor does it perform any regular collection activity.

- The Province has been developing an implementation plan for the establishment of geographic information systems (GIS) throughout Government. These computer systems will allow users to collect, manage and analyze large volumes of data related to geographically referenced data and information. The Department has converted information from the manual Crown Titles System into a digital format for use in a GIS system. However, the Department has been completing the development of this system without an approved Provincial Geomatics Strategy in place. In addition, we noted that the system that was converted contained incomplete Crown Titles information and outdated information with respect to base mapping. As a result, the new digitized information is also

incomplete and outdated.

### **3.27 The Western Health Care Corporation**

The Western Health Care Corporation was constituted under the *Hospitals Act Constitution Order*. The Corporation is responsible for the management and control of the operations of acute and long term care facilities in the western region of the province of Newfoundland and Labrador.

In our report to the House of Assembly for the year ended 31 March 1996 we reported on the results of our review of the Western Memorial Hospital Corporation. In 1996, we concluded that the Western Memorial Hospital Corporation had significant weaknesses in all areas reviewed.

Since our original review in 1996, the Western Health Care Corporation has made improvements in the financial management of the Corporation. These include the improved timeliness of year end financial reporting and the reduction in inappropriate expenditures for employee benefits and travel. However, there are areas that need to be addressed as there are still significant weaknesses. These include:

- Although the Corporation has been provided with \$20.9 million in additional funding during 1998-99, there remains a deficit of \$19.4 million as at 31 March 1999. This is comprised of the 1998-99 operating deficit of \$3.1 million, a \$700,000 capital deficit and a \$15.6 million deficit relating to severance pay and annual leave accruals. The \$15.6 million will have to be funded as it becomes due. The additional funding of \$20.9 million was not intended to continue as part of the annual government contribution.

Expenditures continue to increase at a faster rate than Provincial funding. As a result, deficits will continue to occur unless the Corporation reduces expenditures or the Government increases funding. As at the time of our review (November 1999), the Corporation is projecting a deficit of \$15.7 million in 1999-2000 excluding



depreciation, severance pay and vacation pay.

- Although patient receivables have declined since our previous review in 1996, the percentage of amounts considered collectable has decreased. In 1995, the Western Regional Memorial Hospital estimated that it would collect \$766,000 or 64% of the \$1.2 million owed to it by former patients. However, in 1999, the Corporation estimates that it will collect \$689,000 or 49% of the \$1.4 million owed to it.
- One particular area of concern is the amount due from employees for travel advances and salary advances. These amounts have been advanced to employees as a part of the normal operations of the Corporation; however, the failure to subsequently collect or account for these advances has been a significant weakness.
- Controls over capital assets are not adequate. Capital assets are not physically identified, listed, costed or counted periodically.

Although the Corporation has a computerized database to record maintenance for significant equipment, this database is not kept up to date or monitored to determine which equipment requires maintenance. Maintenance contracts are not listed or monitored to ensure that contracts are renewed as required. As a result, we could not determine whether all equipment is properly maintained.

- The inaccuracies of the computerized inventory records as evidenced by the significant number of differences between the computerized records and the physical counts indicate that controls over inventories need improvement. Our test counts identified variances that could not be reconciled to Corporation records.

### 3.28 Peninsulas Health Care Corporation

The Peninsulas Health Care Corporation was established in January 1996 and operates under the authority of the *Hospitals Act*. Its operations are governed by a Board of Directors comprised of 18 members appointed by the Minister of Health and Community Services. Our review indicated the following:

- The Corporation has incurred deficits each fiscal year since it was established in 1996. The deficit, including non-shareable expenses, as reported in the Corporation's audited financial statements was \$700,000 in 1996-97, \$2.3 million in 1997-98 and \$2.0 million in 1998-99.

In 1997, Government approved a \$20 million health stabilization fund for 1997-98. This resulted in the Corporation receiving a one time payment of \$966,000 which was used to reduce the 1997-98 deficit to the reported \$2.3 million.

When Government approved the payment of \$966,000 from the health stabilization fund, it was expected to eliminate the Corporation's projected deficit of \$889,000 in 1997-98. However, the Corporation experienced difficulty in following its financial plan and as a result, it continued to incur a steadily increasing deficit for the 1997-98 fiscal year. As indicated above, the deficit for 1997-98 was \$2.3 million.

In 1998-99, Government provided an additional \$40 million to eliminate the accumulated deficits of the regional hospital boards as at 31 March 1998. The Corporation received \$3.9 million of this amount toward its accumulated deficit of \$8.4 million at 31 March 1998. The remaining accumulated deficit of \$4.5 million at 31 March 1998 relates to severance pay and annual leave accruals which Government will not fund.

Also, in 1998-99, an additional \$10 million was approved as one time funding to health care boards. The Corporation received \$1 million of this amount; however,

it still had an unfunded deficit of \$2.0 million for 1998-99 which increased the accumulated deficit of \$4.5 million to \$6.5 million.

- The Corporation does not have either a database of maintenance performed on capital equipment or a listing of maintenance contracts relating to each significant piece of capital equipment. As a result, records at the Corporation are not readily available to demonstrate that all significant pieces of equipment are properly maintained.
- In the past two years the Corporation has undertaken a number of studies to address human resource issues such as sick leave, employee moral and communication problems. This is particularly significant since human resource costs represent 76% of the Corporation's expenditures.

The Corporation is having difficulty attracting and retaining salaried doctors. When the Corporation has to retain the services of locum doctors, there are extra costs. For the year ended 31 March 1998, the Corporation spent \$741,000 more than it budgeted for locum doctors and \$500,000 less than budget for salaried physicians. As a result the Corporation spent an additional \$241,000 providing the required service.

Sick leave, including replacement costs, cost the Corporation in excess of \$2 million in each of the past two years. This represented approximately 91,000 hours in 1997-98 (1996-97: 87,500 hours) or 116 hours (1996-97: 115 hours) per full-time position.

- Inefficiencies in management information systems relating to the consolidation of the three predecessor hospital boards in 1996 continue to exist. The Board continues to operate two accounting systems, two inventory systems, two payroll systems and two leave systems. The Corporation is not realizing the economies of scale associated with having one headquarters office to provide

all required administrative and accounting services.

### **3.29 Health and Community Services Boards**

On 1 April 1998, Government transferred programs for community services from the Department of Human Resources and Employment to the Department of Health and Community Services. Effective this same date, Government directed that community service programs including Child Welfare, Community and Corrective Services and Family Rehabilitative Services, be integrated and delivered under the health and community services boards.

There are four health and community services boards in the Province comprised of St. John's, Eastern, Central and Western regions. In addition to the programs transferred from the Department of Human Resources and Employment on 1 April 1998, the health and community services boards provide traditional community health services including health promotion and protection, mental health, continuing care and immunization services.

The financial position and operating results of the four health and community services boards deteriorated significantly in 1998-99. For example, deficits after non-shareable expenses in 1998-99 totalled \$8.7 million before additional funding of \$2.3 million was provided by Government in April 1999. In 1997-98, the four boards reported a net surplus after non-shareable expenses of \$1.2 million. Furthermore, total net assets of the four boards decreased from \$5.4 million in 1997-98 to \$1.5 million in 1998-99.

In addition, the four boards are projecting deficits totalling \$11.8 million for 1999-2000. This \$11.8 million does not include increases in severance and vacation pay which are expected to further increase the deficits. The Department has committed to providing additional funding of \$4.0 million to help fund these deficits which will effectively decrease the projected deficits to \$7.8 million.

### **3.30 Monitoring Hospital Boards**

From 1 November 1994 to 1 January 1996 the Government of Newfoundland and Labrador established eight regional health care institutions boards to administer health care facilities in Newfoundland and Labrador. These boards took over the facilities previously administered by many small local boards.

All eight boards incurred deficits after non-shareable expenses in the 1998-99. Deficits ranged from approximately \$700,000 for Central West Health Care Institutions Board to \$9.0 million for Health Care Corporation of St. John's.

During 1998-99 the Province provided the boards with an additional \$10.0 million to help alleviate the 1998-99 deficits as there were significant deficits in 1999. Despite the additional funding, the boards continued to incur significant operating deficits and only one board, Central West Institutions Board, was able to keep shareable expenditures within the available funding. In addition, our review indicated that all of the boards are projecting significant deficits in 1999-2000.

### **3.31 Sale of Marystown Shipyard Facilities**

Prior to the sale of the shipyard operations, Marystown Shipyard Limited and Vinland Industries, [A Limited Partnership] operated facilities owned by Newfoundland Ocean Enterprises Limited (NOEL). All three companies are 100% owned by the Government of Newfoundland and Labrador.

Operations at Marystown were reported through Marystown Shipyard Limited, with fabrication operations being reported through Vinland Industries, [A Limited Partnership]. All significant capital assets at the facilities were owned directly by NOEL rather than by the operating entities.

Government's involvement with the Marystown shipyard facilities began in 1966 with the construction of the shipyard. The shipyard became operational in 1968, with the fabrication/offshore service facilities being added in 1993 at Cow Head. Both facilities are utilized for construction of new

vessels. Shipyard operations include main hull assembly as well as repair and refit work. The fabrication/offshore service site is used for assembling deck houses and superstructures for new vessels as well as fabrication, repair and service work for offshore semi-submersible rigs, most notably relating to various projects connected with Hibernia development, including work related to the Gravity Base Structure, commonly referred to as the GBS.

In the fall of 1996, Government decided to divest itself of the facilities at Marystown and Cow Head. We were informed that a divestiture information package was prepared and distributed to several companies in the international steel fabrication sector. In June 1997, Friede Goldman International Inc. expressed interest in purchasing the facilities and on 24 September 1997, a Memorandum of Understanding was signed between Government and the company specifying the basic outline of an agreement by which the Province would sell the facilities.

On 22 December 1997, an Asset Purchase Agreement was signed between Government and a new company, Friede Goldman Marystown Ltd., later renamed Friede Goldman Newfoundland Ltd. (FGNL), transferring all of the facilities' assets to this company in exchange for 1,000 of its common shares. The net book value of the assets as disclosed in the audited interim financial statements of Newfoundland Ocean Enterprises Limited as at 31 December 1997 was \$61 million (\$86 million cost less accumulated depreciation of \$25 million).

On 1 January 1998, a Share Purchase Agreement was signed between Government, Friede Goldman Marystown Ltd., Friede Goldman Canada Inc., and Friede Goldman International Inc., to sell all shares of Friede Goldman Marystown Ltd. to Friede Goldman Canada Inc. for \$1.

Not all the conditions included in the sales agreements have been met. In particular, reports relating to man hours of work for the calendar year 1998 and net after tax profits for the 12 months ending March 1998 were not submitted in accordance with agreement provisions. The report relating to man hours of work for 1998, due to be submitted by 28 February 1999, was never

submitted although a Cabinet Committee was provided with this information verbally by company officials in March 1999. The report to indicate the net after tax profits, due to be submitted by 30 June 1998, was not submitted until May 1999.

The Share Purchase Agreement does not require that information provided by Friede Goldman Newfoundland Limited on man hours be audited or otherwise independently verified. The Agreement does provide that the company must retain related information and that Government and its representatives shall have access to such information upon reasonable request and on reasonable notice. Discussions with the Department indicated that the unaudited information provided by the company for 1998 was never verified by Government.

The sales agreements do not require Friede Goldman Newfoundland Limited to meet any employment or other requirements after the term of the agreements has passed, which is 31 December 2000. As well, there is no provision for assets, recorded at a cost of approximately \$86 million at the time the agreements were signed, to return to the Province in the event the company does not comply with the agreements or if the company decided to divest itself of the facilities. In minutes of a Newfoundland Ocean Enterprises Limited/Marystown Shipyard Limited Board meeting held 5 September 1997, it was noted with respect to a discussion held with the Cabinet Committee established to oversee the divestiture, that *"The Cabinet Committee wants the terms of guaranteed employment extended beyond 3 years and wants to incorporate language covering the return of the assets to the Province in the event of certain occurrences."* This was never included in any of the Agreements.

A divestiture information package was prepared and distributed to several companies in the international steel fabrication sector. While the Department did provide a copy of the divestiture information provided to the potential proponents, we were advised that no formal record existed as to whom the divestiture information was provided and the evaluation process followed for any proposals which may have been received.

### 3.32 Newfoundland Government Fund Limited

The Newfoundland Government Fund Limited was incorporated on 10 November 1995 under the *Corporations Act* of the Province of Newfoundland. All shares of the Corporation are held by Ministers of the Crown on behalf of the Province. Its affairs are governed by a Board of Directors which is elected by the shareholders of the Corporation.

The Corporation is a Government-administered venture capital fund under the *Immigration Act* (Canada) and Regulations. Under the Canadian Immigrant Investor Program, the Corporation issued an Offering Memorandum in September of 1996 to raise funds from immigrant investors in order to provide loan and equity capital to establish, expand, purchase, maintain or revitalize businesses or commercial ventures in Newfoundland. For the immigrant investors, in addition to earning a nominal return on their capital, their investment in the Corporation helps satisfy a portion of their visa requirements under Canada's Immigrant Investor Program.

The offering was comprised of units each of which represents a \$250,000 promissory note bearing interest at the simple rate of 2% per annum. Although the promissory note is repayable in full five years from the date on which 70% of the investor proceeds are invested or upon refusal of an investor's Canadian visa application, neither the Government of Canada nor the Government of the Province of Newfoundland offers any guarantees or assurances of a return on an investor's original investment and neither government is liable for any loss or damages that may be suffered by an investor as a result of the investment in the securities. The minimum and maximum amounts of the offering were \$3,500,000 (14 units) and \$35,000,000 (140 units) respectively. The offering expired on 30 June 1998. As of 30 April 1999, Citizenship and Immigration Canada required the Corporation to finalize its investor listing to the maximum offering of 140 units.

Although the Corporation had raised \$13.5 million under the Canadian Immigrant Investor Program to provide capital to businesses and commercial ventures in Newfoundland which



meet the requirements of the Program, the Corporation had been unsuccessful in investing any of the funds as of October 1999. As a result, the Corporation has not complied with the *Immigration Act* (Canada) and Regulations. For example:

- The Corporation has not invested any of the required 70% of the \$13.5 million investment proceeds (or \$9.45 million) in eligible business operations within nine months after the release of the proceeds from the escrow agent; and
- The Corporation has not submitted its annual audited financial statements for the year ended 31 December 1998 to Citizenship and Immigration Canada as of October 1999 although they were required to be submitted by 20 May 1999.

In addition, the Corporation has not complied with the Confidential Offering Memorandum. For example:

- The Corporation has never distributed unaudited interim financial statements to investors by 28 September of each year;
- The Corporation did not submit the annual audited financial statements to the escrow agent in time for distribution to the investors by 30 April of each year;
- The Corporation has not maintained the required 20% of the subscription proceeds (\$2,700,000 up to 30 September 1999) in a repayment account for investment in Canadian liquid securities. At 30 September 1999, the balance in the Corporation's repayment account was \$1,651,088; and
- The Fund had still not exercised its rights as permitted under the Offering Memorandum to have the Escrow agent enforce the requirement that investors make the minimum required deposit and pay the balance within the required time frame.

### **3.33 Royal Newfoundland Constabulary**

On 2 December 1997, a Select Committee of the House of Assembly was appointed to enquire into the arming policy of the Royal Newfoundland Constabulary, and report its findings to the House of Assembly by 31 March 1998. As a result of the recommendations of the Select Committee on the Arming Policy of the Royal Newfoundland Constabulary, members on operational duty were permitted to wear sidearms commencing 14 June 1998. To provide specific direction to members on the control and usage of firearms, the Royal Newfoundland Constabulary issued a revised Firearms Policy at this time. As of November 1999, 620 firearms were maintained by the Royal Newfoundland Constabulary.

One of the recommendations of the Select Committee on the Arming Policy of the Royal Newfoundland Constabulary was also that a firearms audit acceptable to the Minister of Justice be performed annually and submitted to the House of Assembly. To comply with this recommendation, the Chief of Police requested my Office to conduct an audit of firearms. Our review indicated the following:

#### **Control Over Firearms and Ammunition**

The Royal Newfoundland Constabulary has established policies to provide for the management and control of its firearms and ammunition. Controls over firearms at the Royal Newfoundland Constabulary have significantly improved since our review of this area in 1996. Our review, however, identified a number of areas that require improvement. These include the following:

- The firearms and ammunition inventory system is not accurate. Our testing of this system indicated that not all firearms are recorded in the system and certain firearms recorded in the system had already been disposed of.
- Although the inventory system is a perpetual system (i.e. it is updated on an on-going basis), we determined that required adjustments, including dispositions and internal re-assignments of firearms and ammunition, are not always

made on a timely basis. As a result, information on firearms and ammunition inventory is not always accurate and up to date.

- Segregation of duties over the purchasing, accounting and custody of weapons is not adequate. The same individual performs a number of incompatible duties including ordering and receiving of firearms related inventory, maintaining control over both the physical inventory and the inventory information system, and conducting annual inventory counts without any other officials present. Improper segregation of duties may result in errors or unauthorized transactions not being detected.
- In reviewing procedures for the annual physical count, we found that there is no documentation maintained on the results of the count or reasons for any required adjustments between the physical count and recorded inventory. In addition, discussion with Royal Newfoundland Constabulary officials indicated that although adjustments are made to the inventory system, there is no independent review or authorization of these transactions.

### **Adequacy and Compliance of the Firearms Policy**

Our review indicated that the revised Firearms Policy of the Royal Newfoundland Constabulary is comparable to that of the other Canadian police jurisdictions and covered similar issues pertaining to the use and control of firearms.

Our review of compliance with the Firearms Policy indicated that members are not always complying with the policy. For example:

- Some of the plain clothes members on operational duty do not always wear sidearms as required by policy.
- Although policy requires that unloaded firearms be secured in the members personal firearms storage locker at Royal Newfoundland Constabulary facilities or in other approved locations when the member is not on duty, non-compliance

with this policy is regularly observed during monthly inspections.

- Monthly inspections of service firearms are not being conducted as required by policy.
- A significant number of Royal Newfoundland Constabulary members have not requalified in firearms training every 12 months as required by policy. In addition, a significant number of members have not received use of force training as required by policy.

Although Use of Force Reports are required to be prepared by members and reviewed by supervisors to monitor members' compliance with Firearms and Use of Force Policies, we noted that Use of Force Reports are not always being completed and when they are completed, they do not always contain all required information such as member name and type of force used.

In addition, Use of Force Reports are not always submitted to the Use of Force Review Board on a timely basis.

### **3.34 Municipal Debt**

The Department of Municipal and Provincial Affairs is responsible for matters relating to local government, municipal financing, property assessment, urban and rural planning, infrastructure development and engineering, and the coordination of emergency planning for municipalities.

Total municipal debt is comprised of debt owed by municipalities to the Newfoundland Municipal Financing Corporation and to banks. Newfoundland Municipal Financing Corporation is a Crown corporation created by the *Municipal Financing Corporation Act* to provide long-term financing for the capital requirements of municipalities through the issuance of securities and relending the funds to municipalities. The debt incurred by municipalities is used to finance such infrastructure projects as water and sewer systems, and roads. The majority of this debt is cost shared between the Province and the municipalities involved.

Our review disclosed that serious concerns remain with respect to the level of municipal debt, the ability of municipalities to administer this debt, and the monitoring of debt by the Department of Municipal and Provincial Affairs. Specifically, our review disclosed the following:

- The Department could not provide us with the amount of total municipal debt as at 31 December 1998 for the 290 municipalities in the Province, including the three cities. At the time of our review, the Department's records indicated the amount was in excess of \$497 million. Our review of the database of information containing data on total municipal debt revealed that the information was inaccurate and incomplete. Our testing included a review of available audited financial statements for the year ended 31 December 1998 as well as a review of information submitted by the various chartered banks. In comparing this information to the database, several differences and omissions were detected.
- While total debt is increasing, municipal debt financed by the Newfoundland Municipal Financing Corporation is decreasing while the municipal debt financed by chartered banks is increasing. Newfoundland Municipal Financing Corporation debt has decreased from \$445 million as at 31 December 1994 to \$330 million as at 31 December 1998, a reduction of \$115 million.

While municipal debt financed by chartered banks is increasing, the Department does not maintain complete and accurate information on this debt. As a result, the Department does not know the total financial condition of all municipalities.

- Provincial assistance to municipalities, which includes funding for debt servicing costs (principal and interest) and municipal operating grants, has been decreasing while municipal debt costs are increasing. Assistance and infrastructure funding has decreased from \$133 million in 1994-95 to \$110 million in 1998-99.

- Although total debt to the Newfoundland Municipal Financing Corporation has decreased by \$115 million over the last four years, arrears to the Newfoundland Municipal Financing Corporation have increased significantly from \$10.8 million as at 31 December 1993 to \$19.2 million as at 31 December 1998. Since the Department does not have information on all municipal debt at chartered banks, they do not know the extent of arrears, if any.
- For those municipalities for which taxation information was available, mil rates for property taxes ranged from 2.5 mils to 17 mils, water and sewer rates ranged from \$30 to \$420 per household, and poll tax rates ranged from \$20 to \$300.
- The existing *Municipalities Act* outlines a framework of accountability by municipalities to the Department of Municipal and Provincial Affairs. Municipalities are not complying with this framework. For example, most municipalities do not submit their annual budgets by the statutory deadline of 31 December. In addition, 12 municipalities had not submitted the required 1997 financial statements at the time of our review. Financial statements for 1998 were not due to be submitted to the Department by the municipalities at the time of our review and therefore were not generally available. The Department should enforce compliance with the *Municipalities Act* so that it will have the information that is required to monitor the financial condition of the municipalities.

### 3.35 Debt Relief Program

During 1996-97, the Department of Municipal and Provincial Affairs introduced a Debt Relief Program to assist municipalities in debt refinancing or debt restructuring. The Program is intended to assist municipalities in poor financial condition, determined by a comprehensive review of individual municipalities' past performance in relation to financial activities, with consideration of other factors including economic conditions, taxing capacity, and out-migration.

As at 31 March 1999, Government had advanced a total of \$17 million in Program funding to the Newfoundland Municipal Financing Corporation, to be held in a reserve for use in mitigating arrears with respect to municipal loans. The amount of the allocation is determined through assessments completed by the Department with final approval from the Newfoundland Municipal Financing Corporation. Of the \$17 million in Program funding, approximately \$6.1 million had been allocated to 13 municipalities as at 31 March 1999, leaving an unallocated balance in the reserve fund of \$10.9 million.

Our review disclosed that:

- Guidelines for the Program, defining the Program's objectives, organizational structure, processes, and expected outcomes have not been formally established. Draft Program guidelines did exist and were well structured; however, they were not formally approved by the Department. As well, criteria which would determine how much funding a municipality would be entitled to under the program, have not been well defined and properly approved.
- We were advised that the draft guidelines were to be in effect for the period covered by our review; however, certain provisions contained in the draft guidelines were not complied with.
- In April 1997, the Department estimated that it would complete a review of 170 affected municipalities by 30 October 1998. By January 1999, Departmental reviews had commenced with only 112 municipalities, with negotiations being finalized for only 47 of these 112. The Department indicated that the revised estimate for completing the remaining reviews is March 2000.
- The draft guidelines indicated that *"The municipalities that will be targeted are those that spend more than 30% of their municipal revenues on debt."* As well, it is indicated that *"Order of priority will be given to municipalities with the highest debt to revenue ratio but priority may change*

*to accommodate special circumstances."* Our review indicated that the municipalities were not reviewed in this order. For example, of the 20 municipalities with the highest ratio, only 16 had been reviewed as at January 1999 while the review of the remaining 4 had not commenced.

One of the first reviews undertaken was for the Town of Harbour Grace, which was listed as number 153 on the June 1997 list of priority and which had a debt to revenue ratio of less than the 30% targeted under the draft guidelines.

- The negotiated agreements which were signed with the municipalities required that the municipalities must meet certain conditions to access Program funding, including such conditions as raising municipal taxes and not applying for future capital works funding for up to 15 years. In the case of tax increases, the tax rates established by the Department are not consistent and vary by municipality.
- Under the Debt Relief Program, a comprehensive review of each municipality was to be performed incorporating a number of factors, including past performance and the ability to raise revenues and service debt. The analyses completed by the Department did not typically address future capital works and funding requirements. In order for restructuring to be viable on a long term basis, it would be expected that these factors would be taken into account.
- Our review disclosed that a detailed financial analysis was not completed for all municipalities which were reviewed and received funding. Of the 13 municipalities which received funding, the Department did not complete a detailed financial analysis for 2. These 2 municipalities were assisted under the Program with debt relating to water and sewer infrastructure projects which were only partially completed in the past. Due to the fact that the systems were not completed, the intended services were not being provided to the communities involved. Such systems are



considered as dry lines.

For one municipality, the Department considered there was no need to complete a detailed financial analysis as it felt the town was in good financial position. It was indicated that the decision to assume the Council's share of the debt was based on "principle" rather than the financial position of the town as would be expected based on the draft Program guidelines and on the review of other agreements under the Program.

- It is understood from discussions with Departmental officials that the 30% debt to revenue ratio identified in the guidelines was a target and was intended to identify municipalities in need of assistance. However, the lack of definitive indicators as to qualifications for assistance resulted in a process which was not transparent to the various stakeholders involved. In the case of assistance provided under the debt relief program, many municipalities did not receive funding even though their debt to revenue ratio exceeded the 30% identified in the guidelines. As well, many municipalities that did receive funding were left with debt to revenue ratios exceeding 30%.
- Debt Relief Program agreements between the Department and individual municipalities were signed by the Department and the municipalities involved prior to receiving approval from the Department of Finance for allocation from the reserve fund. The Deputy Minister of Finance expressed concerns over such prior approvals in a letter to the Deputy Minister of Municipal and Provincial Affairs.
- Monitoring and reporting mechanisms established to measure success towards achieving Program objectives have not been complied with. In particular, the Debt Relief Program Review Committee indicated to be in place to ensure the program objectives are met, did not hold regular meetings or keep related minutes. Also, although the draft guidelines indicated a need to monitor

the action plans of the individual municipalities, there was no related monitoring strategy in place. As well, other than through ministerial statements, no periodic overview reports were made on the objectives of the Program for the House of Assembly and other stakeholders.

### **3.36 Municipal Capital Works Program**

Municipalities wishing to undertake capital works projects such as water and sewer or road paving must apply to the Department of Municipal and Provincial Affairs for approval under the Municipal Capital Works Program. Interim financing for approved cost shared projects is generally provided to municipalities by the various chartered banks. After completion of the project, the interim bank debt is then typically refinanced through the Newfoundland Municipal Financing Corporation or, in more recent years, through the chartered banks.

Total approved funding for the 1998-99 Program was \$26.6 million. Individual projects approved will be financed by the Newfoundland Municipal Financing Corporation and chartered banks. Each year, Government provides grants to municipalities to help them pay the principal and interest on this debt.

Our review disclosed that:

- Since Cabinet makes the final decision as to which municipal capital works projects are approved for funding by the Province, the information and support for the projects were not made available for my review.
- Our review of the Municipal Capital Works Program indicated that there is no approved, written policy on how the Provincial and municipal cost shared ratios are determined for capital works projects. Prior to 1997, the annual cost sharing arrangements for municipal capital works projects were determined using a formula prescribed in the regulations under the *Municipal Grants Act*. These regulations were discontinued in 1996 with the intention that the formula for funding be replaced by departmental

policy. This was never done.

- Departmental officials informed us that the cost shared ratios depend on the municipality's debt to revenue ratio. However, in 14 of the 20 projects reviewed, the approved cost shared ratio was not consistent with the ratio which would be expected using the criteria indicated by the Department.
- The Department has completed its strategic plan and is currently in the process of developing operational plans for its divisions. Although officials did inform us that policies and procedures relating to the Municipal Capital Works Program are being developed, there was no indication that the calculation of cost sharing ratios would be consistently applied and based on a prescribed formula.

### **3.37 Job Creation Program**

During the fiscal years ended 31 March 1998 and 1999, Cabinet approved funding of \$18.1 million for a special employment initiative known as the Job Creation Program. The purpose of this Program was to create short-term employment throughout the Province. The Program was administered by the following four departments: Municipal and Provincial Affairs, Works, Services and Transportation, Forest Resources and Agrifoods, and Human Resources and Employment.

Funding for the Job Creation Program was not part of the original approved budget for these departments. Instead \$9 million was provided from the Province's Contingency Fund, \$2.6 million was provided through a Special Warrant, and \$6.5 million was transferred from other Government programs.

To coordinate the implementation of the 1998-99 Job Creation Program, Cabinet established a Review Committee. This Committee consisted of the Minister of Municipal and Provincial Affairs, the Minister of Forest Resources and Agrifoods, the Minister of Works, Services and Transportation, a Member of the House of Assembly, and officials of the Department of Municipal and Provincial Affairs. The Committee was

responsible for coordinating the implementation of the Job Creation Program, including all project approvals.

As the Department of Municipal and Provincial Affairs was allocated \$11.1 million or 61% of the total approved funding of \$18.1 million, we limited our review of the Job Creation Program to this Department. Total funding of \$11.1 million allocated to this Department was approved by Cabinet under five separate Job Creation programs throughout the years ended 31 March 1998 and 1999.

The Departmental Review Committee at the Department of Municipal and Provincial Affairs consisted of the Minister of Municipal and Provincial Affairs and three Members of the House of Assembly. In addition, the Department assigned one of its staff as Job Creation Coordinator.

Departmental officials informed us that the Departmental Review Committee established the following program objectives:

- to provide a short term employment response program;
- to support labour intensive job creation initiatives;
- to address the most pressing needs for families and others with no source of employment income;
- to focus on areas of high unemployment where needs are most warranted; and
- to leverage and combine with other programs and fundraising initiatives to supply materials and other non-labor related project components.

Departmental officials also informed us that:

- of the total approved funding of \$11 million, this Review Committee allocated \$10.5 million to the 48 electoral districts;

- the Job Creation Program was not publicly advertised;
- it was incumbent upon each Member of the House of Assembly to advise interested project sponsors of available program funding; and
- all applications for funding within an electoral district are reviewed and approved by that district's Member of the House of Assembly. These applications are then forwarded to the Departmental Review Committee to ensure projects meet Program eligibility criteria.

My review indicated that the Department's administration of the Job Creation Program is not adequate. In particular:

- Project files lacked adequate documentation to support funding decisions and we were often unable to determine if approved applications met established eligibility and selection criteria.
- Additional funding was advanced to project sponsors without project applications being completed and without adequate documentation on how previously approved funds had been spent and how the additional funding is intended to be spent.
- In contravention of the *Financial Administration Act*, the Department made payments for the Job Creation Program from funds approved by the House of Assembly for Special Assistance to municipalities.
- Although project sponsors are required to submit a financial report supporting total project expenditures before the final 25% funding installment is paid by the Department, these funds have often been paid to the sponsor groups prior to the receipt of any financial reports. In general, financial reports were not received by the Department on a timely basis.
- The Department is not receiving adequate information from project sponsors to ensure that program guidelines

were followed and that project funding was used for its intended purpose. For example, documentation to adequately support project expenditures in the form of invoices for materials and payroll records for salaries are generally not provided to the Department.

Ministers of the Crown are responsible for policy development and it is the responsibility of public servants to implement these policies and deliver the Government programs which reflect these policies. I am concerned about the manner in which the Job Creation Program is being delivered. For example, the Program was not publicly advertised and made available to all residents of the Province, funding for the Program has been allocated based on electoral district rather than the merit of applications or other objective assessment, and applications are not subjected to a consistent and rigorous review and evaluation prior to being approved.

I am recommending that Government review the manner in which the Job Creation Program is being delivered.

### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

Of the \$100 million approved under the Canada-Newfoundland Economic Renewal Agreement (ERA) in June 1996, \$22.85 million was allocated to the Tourism Program. This was subsequently increased to \$26.85 million which has been allocated among various projects. As of 31 March 1999, of the \$26.85 million allocated to the Tourism Program, \$20.95 million had been spent.

Our review of the Tourism component of the Canada-Newfoundland Economic Renewal Agreement indicated the following:

- The Management Committee has complied, for the most part, with terms of the Agreement. Our review, however, identified the following weaknesses: advance funding for one project reviewed was provided before the project was formally approved by the Committee, eligible costs were

not adequately defined in all third party contracts, all calls for tenders and announcements on the award of contracts were not approved by the Management Committee, and the Management Committee did not ensure that third parties complied with all relevant Federal and Provincial legislation.

- The Department is not ensuring that all third parties comply with all contract terms including the submission of a three month cash flow when requesting advances and the timely submission of internally prepared financial statements and quarterly status reports.
- The Department has not conducted any inspection or audit on third party records nor has it required any audited financial statements from third parties. As a result, the Department cannot demonstrate that all third party expenditures funded under the Agreement were eligible expenditures.
- The Department is not adequately monitoring all projects as they near completion or as all ERA funds have been disbursed to the third party.
- Although an Evaluation Framework has been established and some useful information is being provided through this Framework, adequate performance information necessary to evaluate the Tourism Program is not being provided by all of the implementing parties. In addition, since key performance targets were not included in the third party contracts there is no formal requirement for these third parties to provide this information. As a result, it will not be possible for the Management Committee to evaluate whether the objectives of the Agreement are being achieved.

### **3.39 Labrador Ferry Service Equipment Repair**

In March 1997 the Province signed an agreement with the Federal government to transfer responsibility for the operation of the coastal Labrador ferry service from Marine Atlantic to the

Province. In exchange for assuming responsibility for the ferry service the Province received \$349.2 million in December 1997, consisting of \$340 million plus accrued interest. As part of the agreement, the Province also received the two ferry vessels used in the operation of the marine freight and passenger services (the MV Northern Ranger and the MV Sir Robert Bonville), several parcels of land together with wharves and related facilities, and other equipment related to the operation of the ferry service including forklifts, fifth wheel trailers and diesel refrigeration units. The main terminal for servicing the equipment used for the coastal Labrador ferry service is Lewisporte.

In order to prepare for the 1998 ferry service season, the Province determined that repairs were required to the equipment it had received from Marine Atlantic. In February 1998, two tenders for the repair of the equipment were issued. The first tender was for the repair of forklifts, fifth wheel trailers, container handlers, a garbage truck, a backhoe, a van and an air compressor. The second tender was for the repair of 52 diesel refrigeration units. Both tenders, with the exception of some minor repairs to the van, were awarded to the same contractor. Total payments to the contractor relating to the two tenders were \$250,000 and \$77,000, respectively.

A further related contract was issued for the provision of various services relating to the former Marine Atlantic premises in Lewisporte. Total payments to the contractor relating to this contract were \$226,000.

### **Tenders**

The Department of Works, Services and Transportation did not comply with the *Public Tender Act* and Government policies relating to the repair of equipment at the Lewisporte ferry terminal. For example:

- (1) The successful tender for repair of the forklifts, fifth wheel trailers, and other ferry terminal equipment was \$11,134. The final cost to complete the work specified in the tender, plus additional work completed by the contractor on the same equipment, totalled approximately \$250,000.



Change orders relating to this tender were not issued in accordance with the *Public Tender Act*.

- (ii) The successful bid for the tendered repair of refrigeration units was \$34.75 per hour. However, most of the work was completed at a rate of \$42 per hour with some at \$52 per hour. The final cost to complete the work specified in the tender totalled approximately \$77,000. The Department had no authority to increase a tendered rate of \$34.75 per hour to \$42 and \$52 per hour.
- (iii) The Department of Works, Services and Transportation contravened the *Public Tender Act* when it did not call public tenders for various other services relating to the former Marine Atlantic premises in Lewisporte. These services cost \$226,000 over a six month period.

The Department of Works, Services and Transportation has weaknesses in its internal control procedures relating to purchasing and payments. Several weaknesses were evident in relation to the Department's payment of invoices including duplicate payment of invoices and payment for goods and services which were not in accordance with the contracts.

## **Chapter 4**

### **Update on Prior Years' Report Items**

This year we continued a process whereby our recommendations are monitored and the results reported within two years of the original report date. This chapter provides the results of this monitoring process relating to the recommendations contained in the *Reports of the Auditor General to the House of Assembly on Reviews of Departments and Crown Agencies for the Years Ended 31 March 1994, 1995, 1996 and 1997*.



**PROVINCE OF NEWFOUNDLAND**

**REPORT OF THE AUDITOR GENERAL**

**TO THE HOUSE OF ASSEMBLY**

**ON THE AUDIT OF**

**THE FINANCIAL STATEMENTS OF THE PROVINCE**

**for the**

**YEAR ENDED**

**31 MARCH 1999**

**PRINTED UNDER THE AUTHORITY OF THE HOUSE OF ASSEMBLY  
ST. JOHN'S, NEWFOUNDLAND**



NEWFOUNDLAND AND LABRADOR

Office of the Auditor General

31 January 2000

The Honourable Lloyd Snow, M.H.A.  
Speaker  
House of Assembly

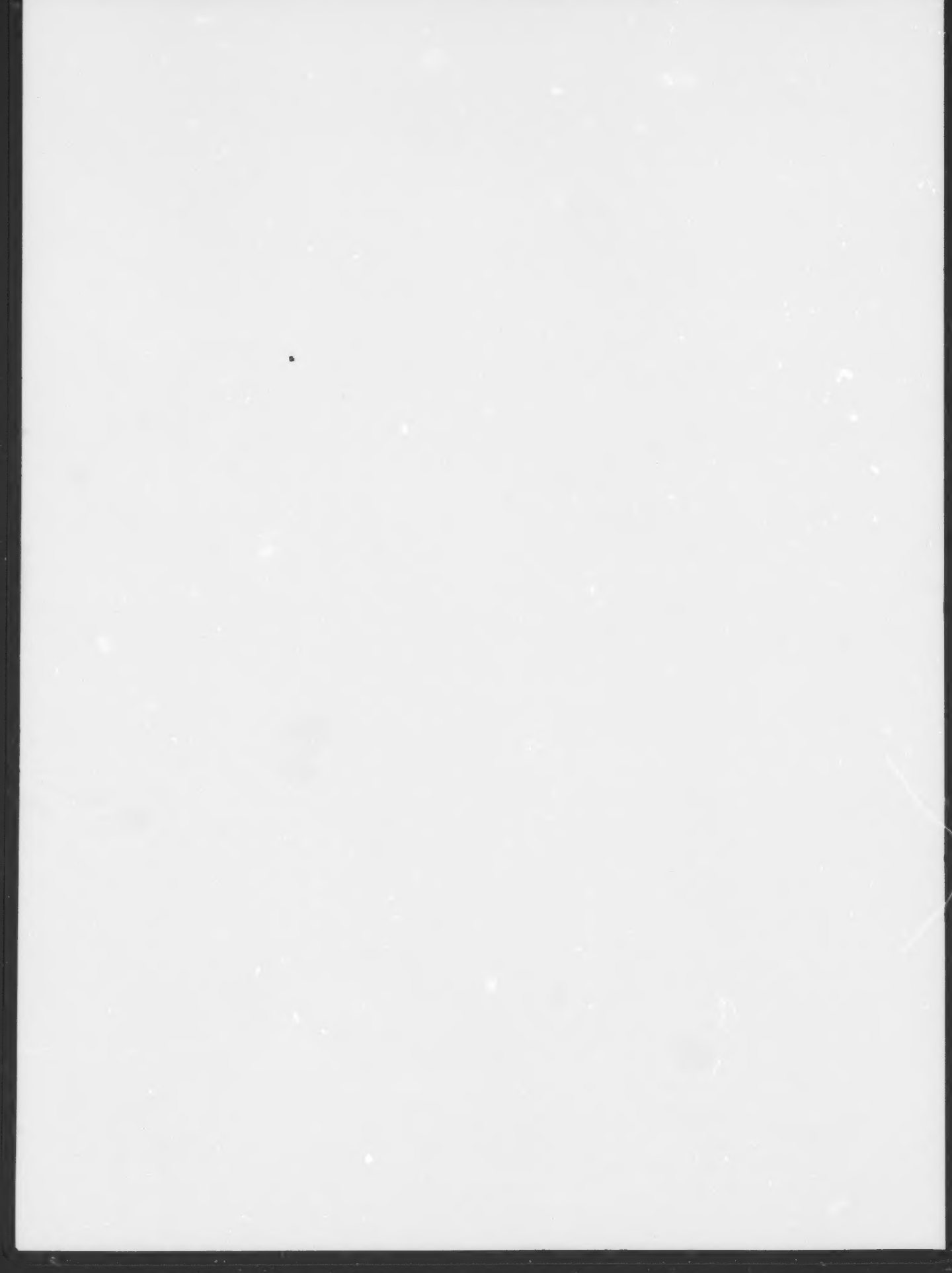
Dear Sir:

In compliance with the *Auditor General Act*, I have the honour to submit herewith, for transmission to the House of Assembly, my Report on the Audit of the Financial Statements of the Province for the year ended 31 March 1999.

Respectfully submitted,

*Elizabeth Marshall*

ELIZABETH MARSHALL, C.A.  
Auditor General



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CHAPTER  
1  
AUDITOR GENERAL'S  
REPORT





# Auditor General's Report

## 1.1 Introduction

This report presents information on the Province's financial statements. The Auditor's Report on the financial statements is presented for the information of the readers. Comments are also provided on the accounting policies used in the preparation of the financial statements and how they compare to the recommendations of the Canadian Institute of Chartered Accountants, which recommends the standards for good practice in financial reporting, accounting and auditing in the public sector.

The Consolidated Summary Financial Statements of the Province provide the most complete information about the operating results and financial position of the Province. These statements consolidate the financial position and results of operation of the Consolidated Revenue Fund, which accounts for the financial activities of central government and the departments, with those of other Government entities. These statements include the operations of all government departments, of which there were 18 in 1998-99, the Legislature, 8 Health Care Corporations, 4 Health and Community Services Boards, 10 School Boards and 42 Crown agencies. These 42 Crown agencies do not include Memorial University of Newfoundland and the Workplace Health, Safety and Compensation Commission.

In this report, I comment on the Consolidated Summary Financial Statements and present a summary of certain financial information contained in these financial statements and the Consolidated Revenue Fund Financial Statements.

## 1.2 Legislative Requirements Relating to the Financial Statements of the Province

In accordance with section 59 of the *Financial Administration Act*, Government prepares a document called the *Public Accounts*. This document includes the Consolidated Summary Financial Statements of the Province and the Consolidated Revenue Fund Financial Statements, and in accordance with the *Act* must show:

- the state of the public debt;
- the revenue and expenditure;
- all compromises, remissions, refunds and amounts written off; and
- those other accounts and statements that may under good accounting practice be required to show the financial position of the Province at the end of the fiscal year.

## Auditor General's Report

Treasury Board prescribes the manner and form in which the Public Accounts of the Province are prepared, as provided for under the *Act*.

Section 11 of the *Auditor General Act* requires that the Auditor General express an opinion as to whether the financial statements included in the Public Accounts present fairly the financial position, results of operations and changes in the financial position of the Province in accordance with the disclosed accounting policies of the Provincial Government and on a basis consistent with that of the preceding year, together with reservations the Auditor General may have.

For the year ended 31 March 1999, the Public Accounts contain the Consolidated Summary Financial Statements, the Auditor General's Report on those financial statements, the Consolidated Revenue Fund Financial Statements, the Auditor General's Report on those financial statements, and other information which Government is required to include or chooses to include.

Since the recommendations of the Canadian Institute of Chartered Accountants relating to financial reporting by governments have now become generally accepted within Canada, section 59 of the *Financial Administration Act* requires compliance with these recommendations to properly present the financial position of the Province at the end of the fiscal year.

### 1.3 Auditor's Report on the Financial Statements of the Province

The Auditor's Report on the Consolidated Summary Financial Statements of the Province for the year ended 31 March 1999 reads as follows:

*To the House of Assembly  
Province of Newfoundland*

*I have audited the consolidated summary statement of financial position of the Province of Newfoundland as at 31 March 1999 and the consolidated summary statements of revenue and expenditure, net debt and changes in financial position for the year then ended. These financial statements are the responsibility of Government. My responsibility is to express an opinion on these financial statements based on my audit.*

*I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles*

## Auditor General's Report

*used and significant estimates made by Government, as well as evaluating the overall financial statement presentation.*

*In my opinion, these consolidated summary financial statements present fairly, in all material respects, the financial position of the Province of Newfoundland as at 31 March 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with the accounting policies disclosed in Note 1 to the consolidated summary financial statements applied on a basis consistent with that of the preceding year.*

*Elizabeth Marshall, C.A.  
Auditor General*

*St. John's, Newfoundland  
23 November 1999*

### 1.4 Government's Results of Operations

For the year ended 31 March 1999, Government's Consolidated Summary Financial Statements reported a deficit of \$163.3 million compared to the 1997-98 reported surplus of \$132.6 million. The 1997-98 surplus of \$132.6 million includes a one time payment of \$347.6 million received from the Federal Government when all responsibility for the operation of the marine, freight and passenger services on and to the coast of Labrador was transferred on 1 April 1997 from the Federal Government to the Province. Had this one-time funding not been received, Government would have reported a deficit of \$215.0 million in 1997-98.

## **Auditor General's Report**

CHAPTER

2

COMMENTS ON

GOVERNMENT'S FINANCIAL REPORTING



## **Comments on Government's Financial Reporting**

### **2.1 Basis of Accounting for Revenues**

Government currently records certain revenues on a modified accrual basis. For example, government records revenue from the Government of Canada tax equalization and personal and corporate income taxes based on regular entitlements for the current year. As adjustments to regular entitlements are subject to future revisions, the revisions are reported in those future years when the adjustments become known. Government does not attempt to provide a reasonable estimate for these future revisions in the periods to which these revisions relate. In addition, revenue from significant provincial taxes, such as Gasoline Tax and Tobacco Tax, are only recorded for those amounts assessed and those taxes collected by vendors up to 31 March but not remitted by that date. Government's financial reporting would be improved if all revenues were recorded on a full accrual basis.

#### **Recommendation**

*Government should consider recording its revenues on a full accrual basis.*

### **2.2 Comparative Budget Figures**

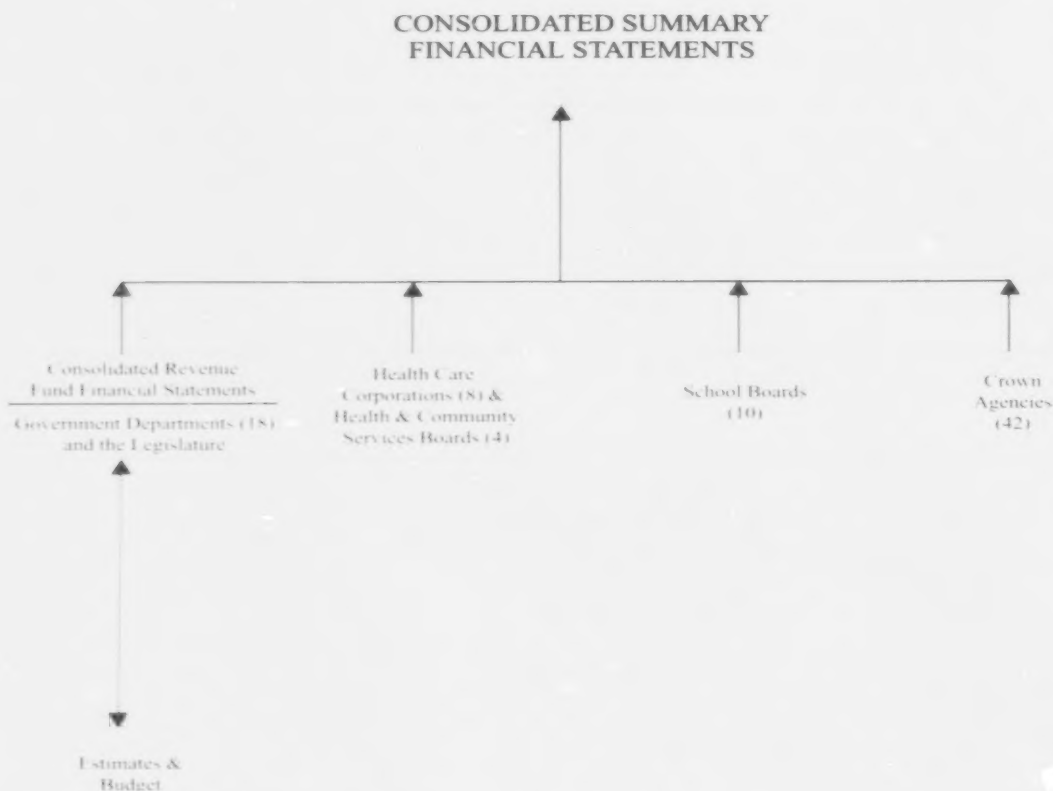
Figure 1 indicates the organizations which are included in Government's Consolidated Summary Financial Statements.

At the present time, and as indicated in Figure 1, Government's annual Estimates and Budget reflect only the activities of the Consolidated Revenue Fund and exclude many significant financial activities of the Province which occur outside the Consolidated Revenue Fund. There is no budget prepared for the Consolidated Summary Financial Statements and, therefore, there is no financial plan against which to compare Government's overall financial position and results of operations.

## Comments on Government's Financial Reporting

Figure 1

### Organizations Included in the Consolidated Summary Financial Statements 31 March 1999



Consolidated summary budgets for government are recommended by the Canadian Institute of Chartered Accountants, the professional body which recommends standards for financial reporting in the public sector. At the present time, the Federal Government and the Provinces of Nova Scotia, New Brunswick, Quebec, Ontario and Alberta publish consolidated summary budgets.

The audited financial statements of the Consolidated Revenue Fund are prepared on the modified accrual basis of accounting while the comparative budget figures are prepared on the modified cash basis. As a



## Comments on Government's Financial Reporting

result, the audited financial statements and the budget of the Consolidated Revenue Fund are not comparable and, as such, diminish the usefulness of the information provided. Although Volume III of the Public Accounts compares actual and budget figures on a modified cash basis, and then reconciles the actual modified cash figures with the actual modified accrual figures in Volume II, this information is not a substitute for preparing a budget on a basis consistent with the actual financial information presented in the audited financial statements of the Consolidated Revenue Fund.

### Recommendations

*Government should prepare a summary budget based on the budgets of all entities included in the Government reporting entity. The summary budget amounts should be prepared on the same basis of accounting as actual results and disclosed in the Consolidated Summary Financial Statements for comparative purposes.*

*Government should prepare the budget for the Consolidated Revenue Fund on the same basis it uses for its accounting.*

## 2.3 Government Reporting Entity

The Canadian Institute of Chartered Accountants has developed criteria for governments to follow in the preparation of consolidated summary financial statements. These criteria require the Province's Consolidated Summary Financial Statements to include all organizations that are accountable for the administration of their financial affairs and resources either to a minister of government or directly to the legislature, and that are owned or controlled by government. A detailed listing of organizations and enterprises included is shown in a schedule to the Consolidated Summary Financial Statements of the Province.

The Consolidated Summary Financial Statements include organizations and enterprises that meet the criteria for inclusion, with the exception of the Workplace Health, Safety and Compensation Commission and Memorial University of Newfoundland, both of which meet the criteria.

Our review of the *Workers' Compensation Act* indicates the Commission is accountable to and controlled by Government. The *Act*, however, does not deal with ownership of the Commission and responsibility for its unfunded liability, which at 31 December 1998 was \$111.1 million. The criteria of accountability and control are sufficient to warrant inclusion in the reporting entity. A note to the Schedule of Trust Accounts in the Consolidated Summary Financial Statements for the year ended 31 March 1999 indicated that Government considered the Commission to be a form of trust. This note disclosed information on the Commission's

## Comments on Government's Financial Reporting

deficit and unfunded liability for the year ended 31 December 1998. The provinces of Saskatchewan, Manitoba, Quebec and New Brunswick include their workers' compensation boards in their government's financial statements. Prince Edward Island provides note disclosure and in British Columbia, Ontario and Nova Scotia it is structured as a trust and is therefore excluded.

Our review of the *Memorial University Act* indicates that the University is accountable to and controlled by Government. While most other provinces have not included universities in their consolidated summary financial statements, it is noted that in British Columbia, the Auditor General recently expressed a qualified opinion regarding the decision by the Government of that Province to reverse the prior inclusion of universities in its Summary Financial Statements. In most other jurisdictions, Auditors General have expressed concerns similar to ours relating to the exclusion of universities from the government reporting entity.

### Recommendation

*The Workplace Health, Safety and Compensation Commission and the Memorial University of Newfoundland should be included in the Government reporting entity.*

## 2.4 Tangible Capital Assets

In September 1997, the Canadian Institute of Chartered Accountants (CICA) issued the accounting and reporting standards for the tangible capital assets of governments. Tangible capital assets include such items as roads, buildings, vehicles, equipment, land, water systems, aircraft, computer hardware and software, dams, canals and bridges.

In accordance with these accounting and reporting standards, tangible capital assets should be accounted for and reported as assets on a Statement of Tangible Capital Assets at cost. For each major category of tangible capital assets, the Statement of Tangible Capital Assets should disclose cost, additions, disposals, the amount of any write-downs in the period, the amount of amortization of the costs of tangible capital assets for the period, accumulated amortization, the amortization method and rate used, and the net book value.

As provided by CICA standards, governments may report their financial results on either the expense basis or expenditure basis of accounting. The choice of the accounting basis affects how tangible capital assets are accounted for and reported in governments financial statements as indicated in Figure 1.

## Comments on Government's Financial Reporting

Figure 1

### Tangible Capital Assets Basis of Accounting

| Expense Basis                                                                                                                                               | Expenditure Basis                                                                                                                |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------|
| Cost of the asset is reported on the Statement of Financial Position.                                                                                       | Cost of the asset is reported only on the Statement of Tangible Capital Assets and not on the Statement of Financial Position.   |
| Amortization is accounted for as an expense in the Statement of Operations.                                                                                 | Amortization is reported only on the Statement of Tangible Capital Assets and not on the Statement of Revenue and Expenditures.  |
| The net write-down is accounted for as an expense in the Statement of Operations.                                                                           | The write-down is reported only on the Statement of Tangible Capital Assets and not on the Statement of Revenue and Expenditure. |
| The difference between the proceeds on disposal and the net book value of the asset is accounted for as a revenue or expense in the Statement of Operation. | The net proceeds on disposal of an asset is accounted for as revenue in the Statement of Revenue and Expenditure.                |

Source: CICA Handbook

The Province reports its capital assets on the expenditure basis. As a result, tangible capital assets are currently not valued for presentation on the Statement of Assets and Liabilities in the Consolidated Revenue Fund Financial Statements but are expensed in the year of acquisition or construction. The Consolidated Revenue Fund Financial Statements do, however, include a Schedule of Tangible Capital Assets which provides information for various categories of tangible capital assets such as the estimated cost of additions and disposals, estimated useful life, annual and accumulated amortization, and net book value. This Schedule includes those tangible capital assets having an estimated individual historic cost in excess of \$100,000.

While the Province has continued its efforts to accumulate information on all of its tangible capital assets, to comply with CICA recommendations for tangible capital assets several issues must be addressed. These issues include the incompleteness of information on capital assets disclosed in the Schedule, the lack of an accounting system to record information on capital assets, and the lack of clear and documented criteria and guidelines for the definition of a capital asset and the relevant costs to be included in this definition.

## **Comments on Government's Financial Reporting**

The Province has indicated that it is continuing efforts to improve the completeness and reasonableness of the cost estimates of tangible capital assets and will examine the process for capital asset recording and reporting in the province's financial statements.

### **Recommendation**

*Government should continue with its efforts to improve the completeness and accuracy of its capital assets.*

## **2.5 Periodic Financial Statements**

Government's financial statements are an important component of its financial management system and should show the results of operations and its financial position on a periodic basis. Periodic financial statements are important to effectively monitor and control government operations. Currently, neither monthly nor quarterly financial statements are prepared by Government to determine its results of operations and its financial position on an on-going basis. Rather, Government only prepares annual financial statements.

We indicated last year that Government was implementing a system which was expected to address the concerns related to periodic reporting. During 1998-99, Government implemented the new Financial Management System which included the following five core applications: budgeting, purchasing, accounts payable, accounts receivable, and general ledger. All core applications are fully operational, with the exception of the accounts receivable component which is anticipated to become fully operational during 2000-2001.

In addition to these core applications, however, other financial systems are maintained independent of the Financial Management System including the Human Resource Management Information System (payroll), payments to one-time vendors, Motor Registration Division System, Taxation Information Management System and the Inventory Management System. Information from these other systems are processed into the Financial Management System through the use of computer interfaces. However, Government is still not preparing periodic financial statements.

### **Recommendation**

*Government should prepare periodic financial statements.*

## Comments on Government's Financial Reporting

### 2.6 Timeliness of the Province's Financial Statements

In order for financial statements to be useful, they have to provide relevant and reliable information on a timely basis. Traditionally, Government has tabled its financial statements in December, nine months after the year end. In previous years, we recommended to Government that its financial statements be prepared on a more timely basis so as to provide the users with current financial information. Figure 1 provides the dates that the Consolidated Summary Financial Statements for the years ended 31 March 1997, 1998, and 1999 were released for the 11 jurisdictions in Canada.

**Figure 1**

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**Consolidated Summary Financial Statements  
Release Dates  
Years Ended 31 March**

| <b>Jurisdiction</b>  | <b>1997</b>      | <b>1998</b>       | <b>1999</b>                 |
|----------------------|------------------|-------------------|-----------------------------|
| Newfoundland         | 18 December 1997 | 15 December 1998  | 14 December 1999            |
| Nova Scotia          | 7 August 1997    | 31 July 1998      | 15 December 1999            |
| Prince Edward Island | 30 January 1998  | 17 December 1998  | 7 December 1999             |
| New Brunswick        | 13 August 1997   | 24 September 1998 | 29 December 1999            |
| Quebec               | Not Produced     | 17 June 1999      | Not Released at Report Date |
| Ontario              | 9 September 1997 | 28 September 1998 | 15 October 1999             |
| Manitoba             | 31 October 1997  | 30 November 1998  | 29 November 1999            |
| Saskatchewan         | 4 September 1997 | 27 August 1998    | 28 October 1999             |
| Alberta              | 26 June 1997     | 24 June 1998      | 28 June 1999                |
| British Columbia     | 18 December 1997 | 20 October 1998   | 16 September 1999           |
| Canada               | 15 October 1997  | 15 October 1998   | 26 October 1999             |

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Figure 2 provides the dates that the Consolidated Revenue Fund Financial Statements for the years ended 31 March 1997, 1998, and 1999 were released for the 11 jurisdictions in Canada.

## Comments on Government's Financial Reporting

Figure 2

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**Consolidated Revenue Fund Financial Statements  
Release Dates  
Years Ended 31 March**

| <b>Jurisdiction</b>  | <b>1997</b>       | <b>1998</b>       | <b>1999</b>                 |
|----------------------|-------------------|-------------------|-----------------------------|
| Newfoundland         | 18 December 1997  | 15 December 1998  | 14 December 1999            |
| Nova Scotia          | 7 August 1997     | 31 July 1998      | Not produced                |
| Prince Edward Island | 30 January 1998   | 17 December 1998  | 7 December 1999             |
| New Brunswick        | Unaudited         | Unaudited         | Unaudited                   |
| Quebec               | 18 December 1997  | 17 June 1999      | Not Released at Report Date |
| Ontario              | 9 September 1997  | 28 September 1998 | Not produced                |
| Manitoba             | 17 September 1997 | 28 September 1998 | 30 September 1999           |
| Saskatchewan         | 4 September 1997  | 27 August 1998    | 28 October 1999             |
| Alberta              | 24 September 1997 | 30 September 1998 | Not produced                |
| British Columbia     | 18 December 1997  | 20 October 1998   | 16 September 1999           |
| Canada               | 28 October 1997   | 17 November 1998  | Not produced                |

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We received the first draft of the Consolidated Revenue Fund Financial Statements and the Consolidated Summary Financial Statements for the year ended 31 March 1999, on 9 August 1999 and 8 October 1999 respectively. In my opinion this annual reporting is not timely and does not facilitate effective financial management of the Province.

### **Recommendation**

*Government should prepare its financial statements on a timely basis.*

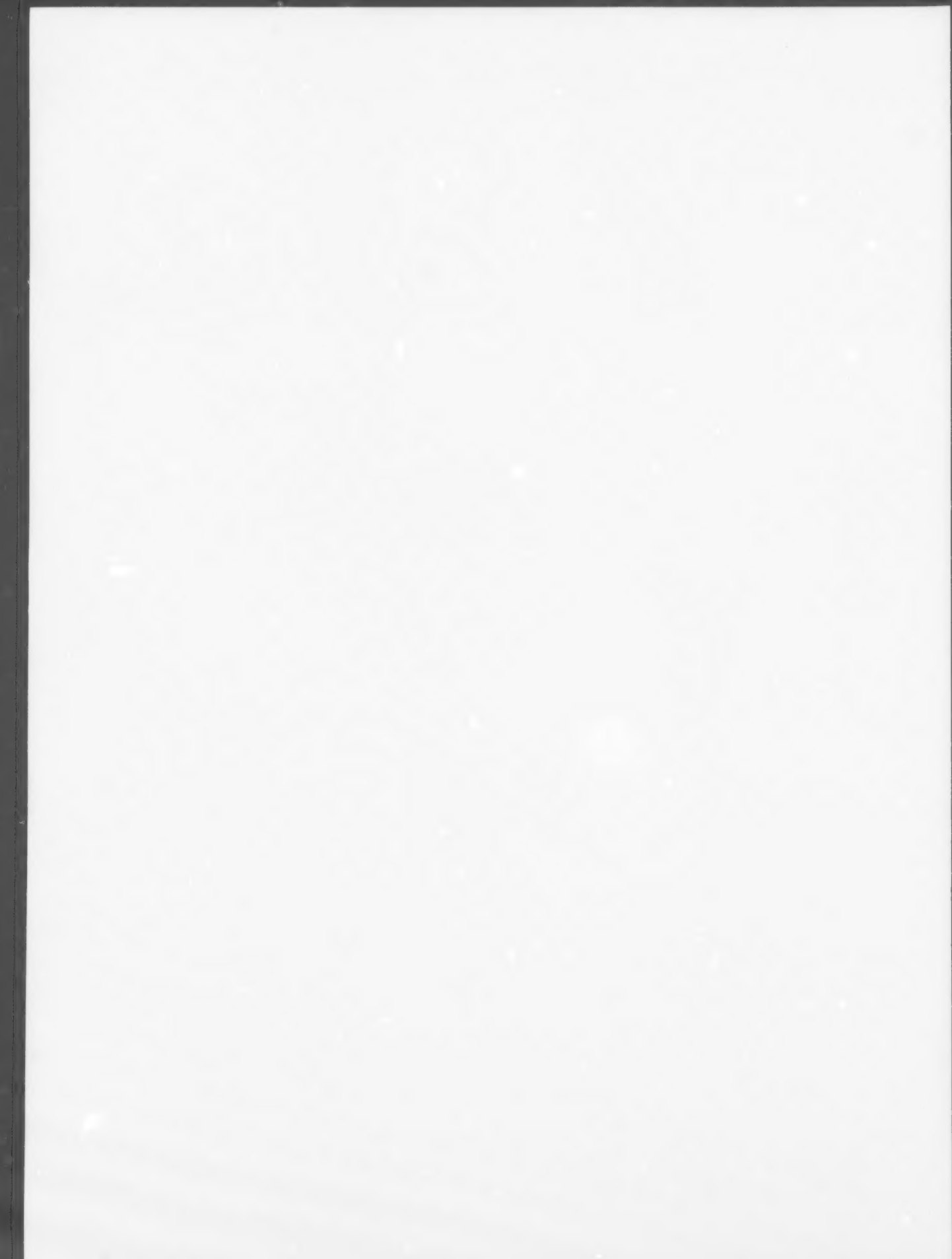
CHAPTER

3

COMMENTS ON

SELECTED FINANCIAL INFORMATION







## Comments on Selected Financial Information

### 3.1 Key Indicators of the State of a Government's Finances

The Canadian Institute of Chartered Accountants is the professional body that recommends standards for financial reporting, accounting and auditing in the public sector. It also initiates research studies on public sector accounting and auditing matters.

In 1997, the Canadian Institute of Chartered Accountants issued a Research Report entitled *Indicators of Government Financial Condition*. That report explored a variety of financial indicators and identified ten which it felt best describes the financial condition of a government. These ten indicators were categorized in terms of three elements of financial condition - sustainability, flexibility, and vulnerability.

#### (i) Sustainability

Sustainability is the degree to which a government can maintain existing programs and meet existing creditor requirements without increasing the debt burden on the economy. The research study proposes that users of the province's financial statements look at the long-term trends in two indicators:

- deficit to GDP; and
- debt to GDP.

For purposes of this Report, I have presented the debt to GDP ratio over the past five years. This ratio measures Government's debt position relative to the Province's economic base. If the Province's debt grows faster than the Provincial GDP, the ratio will increase and become less favorable, indicating that the debt burden is becoming more onerous. Conversely, a declining debt to GDP ratio is positive as it indicates that the debt burden is becoming less onerous. While it is difficult to determine an appropriate level of debt, it is positive that the debt to GDP ratio has mainly declined over the past five years, as indicated in Section 3.4, Figure 6, on page 29 of this Report.

#### (ii) Flexibility

Flexibility is the degree to which a government can increase its financial resources to respond to rising commitments by either expanding its revenues or increasing its debt. The research study proposes that users of the province's financial statements look at the long-term trends of three indicators:

- interest costs as a percentage of total revenue;

## Comments on Selected Financial Information

- changes in physical capital stock; and
- own source revenues to GDP.

For purposes of this Report, I have presented interest costs as a percentage of total revenue to indicate the extent to which Government revenues are used to pay the interest on the Province's debt. As indicated in Section 3.4, Figure 5, on page 28 of this Report, interest costs on borrowings as a percentage of total revenue has declined in recent years but increased again in 1999. As indicated in Section 3.4, Figure 9, on page 31 of this Report, the province's net debt (excluding the unfunded pension liability) is \$5.557 billion.

### (iii) Vulnerability

Vulnerability is the degree to which a government becomes dependent on, and therefore vulnerable to, sources of funding outside its control or influence. In 1998-99, the Federal Government provided \$1.860 billion of the Province's total revenue of \$3.785 billion.

The research study proposed that users of the province's financial statements look at the long term trends of five indicators:

- government-to-government transfers compared to own source revenues;
- foreign-held government debt to net government debt;
- foreign currency debt to net government debt;
- current account balance to GDP; and
- total external debt to GDP.

For purposes of this Report, we present two indicators. Figure 1 on the following page indicates the percentage of Federal revenues compared to the Province's revenues from its own sources. As the figure indicates, over the past five years, Federal revenues ranged from 43.0% in 1997 to 50.5% in 1998. For 1999, Federal revenues accounted for 49.1% of the Province's total revenues.

## Comments on Selected Financial Information

**Figure 1**

**Consolidated Summary Financial Statements**  
**Federal Revenues as a Percentage of Total Revenues**  
**Years ended 31 March**

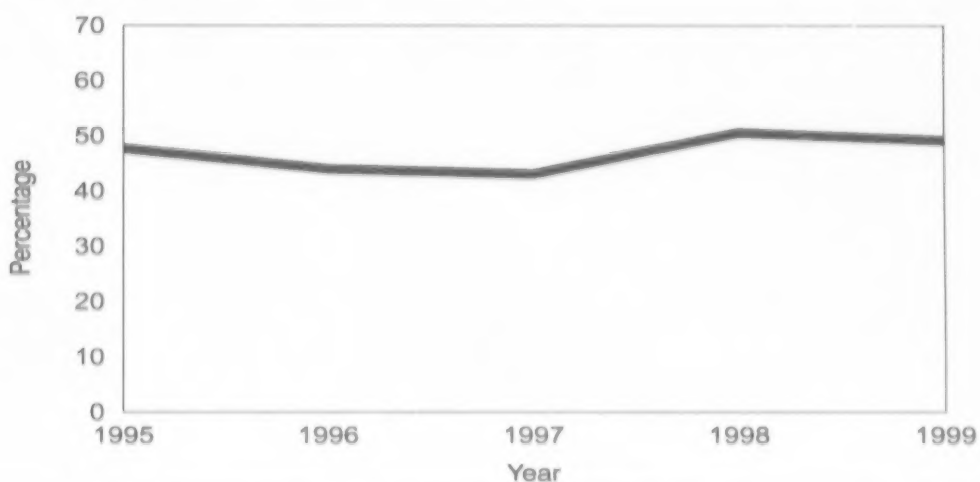
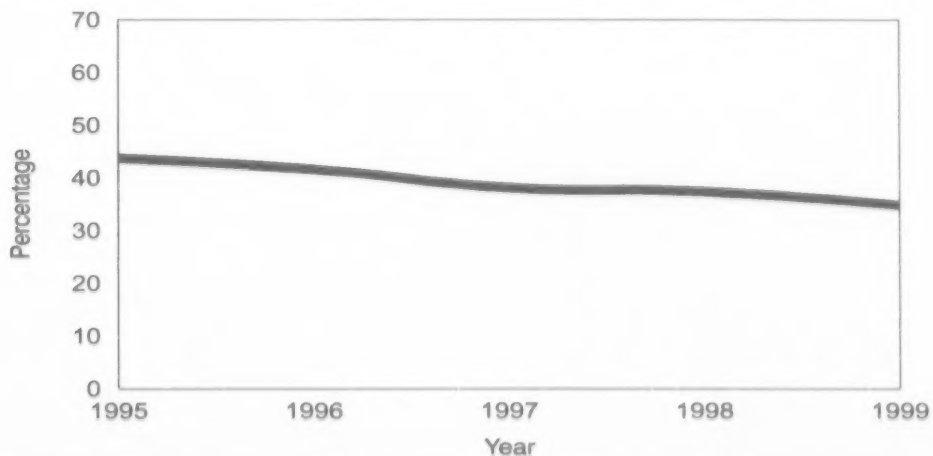


Figure 2 compares the province's foreign currency debt to the province's total debt, and indicates the degree of vulnerability which the Province has to currency swings. As the figure indicates, at 31 March 1999, 35 % of the Province's debt is in foreign currencies.

**Figure 2**

**Consolidated Summary Financial Statements**  
**Foreign Currency Debt as a Percentage of Total Debt**  
**Years ended 31 March**



## Comments on Selected Financial Information

As at 31 March 1999 the Province has \$2,317 million in foreign debt and as a result is vulnerable to currency swings. For example, if the value of the Canadian dollar decreases from 66 cents U.S. to 65 cents U.S., the \$1,173 million in U.S. debt outstanding as at 31 March 1999, when translated into Canadian dollars, would increase by \$27 million Canadian (i.e. from \$1,770 million Canadian to \$1,797 million Canadian).

### 3.2 Amounts Owing to Government

Government policy requires that an accounts receivable system be maintained by Government departments, that departments ensure all receivables are properly recorded in their books of account and that collection be actively pursued.

Figure 1 outlines information on accounts and taxes receivable, and loans, advances and mortgages receivable, and the related allowances for doubtful accounts as disclosed in the Consolidated Revenue Fund Financial Statements for the year ended 31 March 1999. This figure also includes the amount Government has written off during the past five years related to these accounts. In addition to the accounts written off in Figure 1, Government has also written off \$10.84 million in tax forgiveness and \$11.77 million in tax remissions.

Figure 1

**Consolidated Revenue Fund**  
**Accounts, Taxes, Loans, Advances and Mortgages Receivable**  
**Years Ended 31 March**  
**(\$000's)**

|                                                    | 1995      | 1996      | 1997      | 1998      | 1999      | Total     |
|----------------------------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|
| Total Receivables                                  | \$551,764 | \$537,153 | \$474,797 | \$461,612 | \$471,466 |           |
| Less: Amounts<br>Considered to be<br>Uncollectible | 279,065   | 279,924   | 215,210   | 211,832   | 242,344   |           |
| Net Receivables                                    | \$272,699 | \$257,229 | \$259,587 | \$249,780 | \$229,122 |           |
| Accounts Written off                               | \$ 5,398  | \$ 20,790 | \$ 69,877 | \$ 7,972  | \$ 1,855  | \$105,892 |

The Canadian Institute of Chartered Accountants (CICA) recommends how to account for and report loans receivable in government financial statements, giving particular attention to special characteristics that distinguish them from commercial loans made in the private sector.

## Comments on Selected Financial Information

The CICA defines a loan receivable as a financial asset of a government represented by a promise by a borrower to repay a specific amount at a specified time or times, or on demand, usually with interest. Key to this definition is the fact that financial assets provide resources to discharge existing liabilities or finance future operations.

The CICA has recommended that when a direct relationship can be established between the repayment of a loan and a government's funding to the borrower, the portion of the loan that is expected to be recovered from future appropriations from government should be accounted for as an expenditure. When the terms of a loan are so concessionary that the substance of the transaction is that all or a significant part of the loan is more in the nature of a grant, the grant portion of the transaction should be recognized as an expenditure when the loan is made. A loan receivable should be removed from a government's statement of financial position when it has been repaid, the risks and rewards associated with the loan have been transferred, the right to repayment has expired or been waived, or it is written off.

A number of the recommendations made by the CICA apply to the accounting policies of Government and should be considered in preparing the financial statements. These include the following:

- The CICA describes a loan receivable as a financial asset of a government represented by a promise by a borrower to repay a specific amount, at a specified time or times, or on demand, and usually with interest. Loans being established where there may not be a reasonable expectation of recovery would not qualify as a financial asset. In the 1998-99 fiscal year, \$7.8 million (1997-98 - \$99,000) of new loans were established for payments made by the Province to honour guarantees it provided on debt. All of these new loans were recorded as assets of the Province while also being added to its allowance for doubtful accounts.
- The CICA recommends that when the terms of a loan are so concessionary that the substance of the transaction is that all or a significant part of the loan is more in the nature of a grant, the grant portion should be recognized as an expenditure when the loan is made. During the year, advances totalling \$507,758 (1997-98 - \$507,758) were made to Newco IV Corporation and had been recorded as a loan receivable even though there were no specified repayment terms. However, the \$507,758 has been recorded in the Province's allowance for doubtful accounts.
- The CICA provides guidance as to the proper disclosure of loans receivable. Currently, the Province's financial statements do not disclose such items as the repayment terms, interest terms and

## Comments on Selected Financial Information

security held for any of its loans and advances receivable as recommended by CICA.

### Crown Lending Agencies

The Province of Newfoundland lends money to individuals, organizations and local governments to achieve policy objectives and, to a lesser extent, to earn a return on the use of government funds. These loans may be used to support regional development and provide economic assistance to those who qualify.

The Statement of Financial Position of the Consolidated Revenue Fund as at 31 March 1999 disclosed loans, advances and mortgages receivable of \$226.7 million (1998 - \$227.4 million), less an allowance for doubtful accounts of \$160.6 million (1998 - \$135.6 million). Figure 2 discloses the composition of these loans, advances and mortgages receivable.

Figure 2

**Consolidated Revenue Fund**  
**Composition of Loans, Advances and Mortgages Receivable**  
**31 March 1999**  
**(\$ Millions)**



Source: 31 March 1999 Loans, Advances and Mortgages Receivable Schedule, Consolidated Revenue Fund

## Comments on Selected Financial Information

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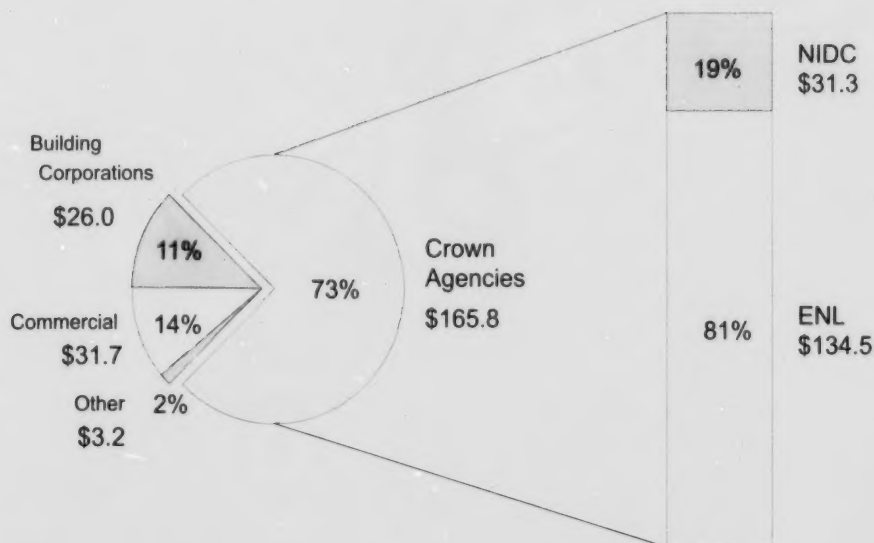
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Figure 2

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**Composition of Loans, Advances and Mortgages Receivable**  
**31 March 1999**  
**(\$ Millions)**



Source: 31 March 1999 Loans, Advances and Mortgages Receivable Schedule, Consolidated Revenue Fund



## Comments on Selected Financial Information

The funds advanced to the Crown lending agencies by the Province are in turn lent to individuals and corporations. Three of these Crown agencies account for 59% of the Province's loans, advances and mortgages receivable. These agencies are listed in Figure 3 along with their loan and equity portfolios.

**Figure 3**

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**Loan and Equity Portfolios of Crown Agencies**  
**Years Ended 31 March**  
**(\$ 000's)**

| <b>Crown Agency</b>                              | <b>1998</b>      | <b>1999<br/>(unaudited)</b> |
|--------------------------------------------------|------------------|-----------------------------|
| Enterprise Newfoundland and Labrador Corporation | \$ 78,046        | \$ 76,598                   |
| Farm Development Loan Board                      | 9,527            | 8,872                       |
| Fisheries Loan Board                             | 32,539           | 27,154                      |
| <b>Total</b>                                     | <b>\$120,112</b> | <b>\$112,624</b>            |

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Source: 31 March 1999 draft financial statements of Crown agencies

In 1994 we completed a review of the financial statements of Enterprise Newfoundland and Labrador Corporation and its predecessor agencies, as well as the Farm Development Loan Board and the Fisheries Loan Board to determine:

- total loans issued, including interest, as disclosed in their respective financial statements;
- amounts repaid;
- amounts written off;
- balances outstanding; and
- amounts deemed uncollectible.

As at 31 March 1979, the predecessor entities of Enterprise Newfoundland and Labrador Corporation (ENL), the Farm Development Loan Board (FDLB) and the Fisheries Loan Board (FLB) had a combined loan and equity portfolio of approximately \$48.5 million. To 31 March 1999, an



## Comments on Selected Financial Information

additional \$484.0 million in loans and interest have been added to the portfolios. Of this \$532.5 million portfolio, 67% has been repaid, 29% was written off or considered uncollectible and a net receivable of 4% is still outstanding. Figure 4 summarizes these amounts by entity.

Figure 4

### Loan and Equity Portfolios of Crown Agencies Summary of Findings (\$ Millions)

| Agency | 31 March 1979<br>Balance | 1979-99<br>Loans,<br>Equity<br>and<br>Interest | Amount<br>Repaid | Amounts<br>Written<br>Off | 31 March 1999<br>Balance | Amounts<br>Considered<br>Uncollectible | Percent of<br>Accounts<br>Written Off or<br>Considered<br>Uncollectible |
|--------|--------------------------|------------------------------------------------|------------------|---------------------------|--------------------------|----------------------------------------|-------------------------------------------------------------------------|
| ENL    | \$ 22.1                  | \$268.4                                        | \$168.8          | \$45.1                    | \$ 76.6                  | \$61.4                                 | 36.7%                                                                   |
| FDLB   | 2.1                      | 41.3                                           | 33.3             | 1.2                       | 8.9                      | 5.3                                    | 15.0%                                                                   |
| FLB    | 24.3                     | 174.3                                          | 152.0            | 19.5                      | 27.1                     | 23.5                                   | 21.7%                                                                   |
| Total  | \$ 48.5                  | \$484.0                                        | \$354.1          | \$65.8                    | \$112.6                  | \$90.2                                 | 29.3%                                                                   |

Source: 1979-1998 audited financial statements and 31 March 1999 unaudited financial statements

### 3.3 Employee Pension Obligations

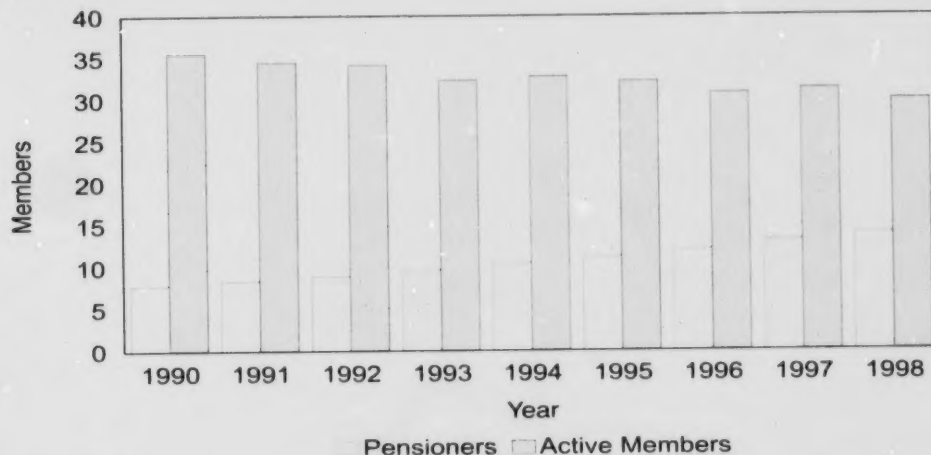
Prior to 1967, public service salaries and pension benefits were paid under the authority of the *Civil Service Act*. Under that legislation there were no employee or employer contributions to a pension plan and pension benefits were paid out of the Consolidated Revenue Fund. In 1967, legislation was enacted which required that employees contribute to a pension plan. Employees' pension premiums were paid into the Consolidated Revenue Fund and pension benefits continued to be paid out of it.

In 1981, legislation was enacted which created the Province of Newfoundland Pooled Pension Fund and required that employee and employer pension premium contributions be paid into the Fund. Subsequent to the establishment of the Fund, pension benefits were paid by the Fund irrespective of whether the employee had contributed pension premiums to it. Figure 1 provides historical data for the Fund relating to pensioners and active members for the past nine years.

## Comments on Selected Financial Information

Figure 1

**Province of Newfoundland Pooled Pension Fund  
Population History: Pensioners and Active Members  
Years Ended 31 December  
(000's)**



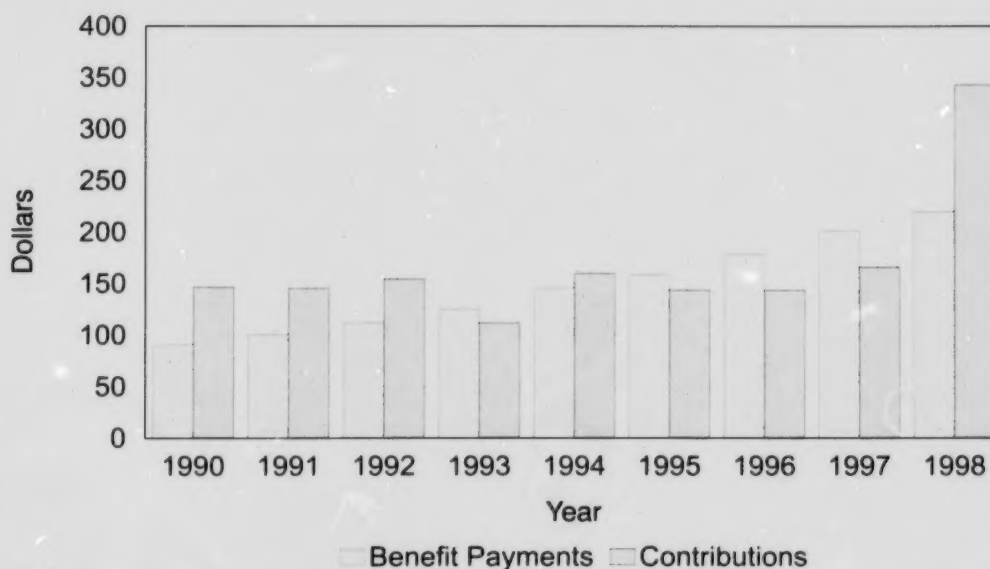
The Province of Newfoundland Pooled Pension Fund is comprised of four pension plans: the Public Service Pension Plan, the Teachers' Pension Plan, the Uniformed Services Pension Plan, and the Members of the House of Assembly Pension Plan. All employee and employer contributions are deposited into the Fund and pension benefits to plan members and other pension payments are made from it.

Our review disclosed that for the year ended 31 December 1998, approximately 30,000 employees, Members of the House of Assembly, and the employer paid pension premiums totalling \$343 million into the Pension Fund under the four pension plans. Premiums of \$343 million include a \$196 million contribution by the employer in excess of matching provisions. During the same period, the Fund provided benefits totalling \$220 million to approximately 14,000 retirees. Figure 2 provides historical data for the Fund relating to pension benefits paid and pension contributions received for the past nine years.

## Comments on Selected Financial Information

Figure 2

**Province of Newfoundland Pooled Pension Fund  
Pension Benefit Payments and Contributions  
Years Ended 31 December  
(\$ Millions)**



Commencing during the 1997-98 fiscal year, Government started to make special payments to the Public Service Pension Plan to address the unfunded liability which at 31 March 1998 was \$1.306 billion and by 31 March 1999 had decreased to \$1.043 billion. Government contributed \$30 million in each of 1997-98 and 1998-99. In 1999-2000 Government indicated that it will continue with payments of at least \$40 million per year until the pre-1980 debt is repaid. In addition, Government has increased the contributions for employees and employers over the next four years. These actions are expected to extend the life of the Plan beyond the year 2030.

During 1998-99, Government negotiated a new collective agreement with the Newfoundland and Labrador Teachers' Association which included provisions to address the unfunded liability of the Teachers' Pension Plan which as of 31 March 1998 was \$1.764 billion and by 31 March 1999 had decreased to \$1.607 billion. In accordance with the agreement, Government will contribute up to \$815 million to the Plan over a 14 year period. Government paid \$166 million toward this commitment in September 1998 and a further payment of \$166 million in September

## Comments on Selected Financial Information

1999. Additional annual payments are to be made in instalments of \$76 million over a 12 year period commencing on or before 1 September 2000 and contributions rates for all teachers and the Government were increased by 0.5% effective 1 September 1998.

The Uniformed Services Pension Plan and the Members of the House of Assembly Pension Plan have no assets. In the case of the Uniformed Services Plan, the pension liability will increase from the present \$191.9 million to an estimated \$349.0 million in 2026. In the case of the Members of the House of Assembly Pension Plan the pension liability will increase from the present \$46.9 million to an estimated \$73.2 million in 2016.

In the Annual Reports to the House of Assembly for the years ended 31 March 1993 to 1998, I recommended that Government address its unfunded pension liability. Government has taken action to address the unfunded liability of the Public Service Pension Plan and the unfunded liability of the Teachers' Pension Plan. While these measures will favorably impact the unfunded liabilities, I am still concerned with the extent of the Province's overall unfunded liability which as at 31 March 1999 was \$2.888 billion.

### Recommendation

*Government should continue its efforts to address its unfunded pension liability.*

## 3.4 Debt

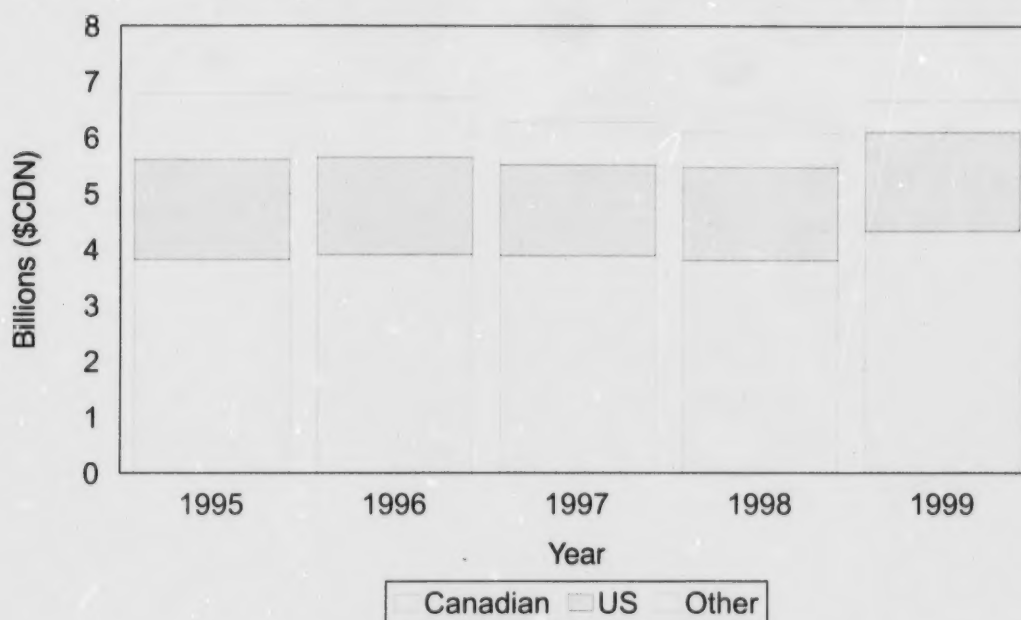
As at 31 March 1999, total borrowings were reported in the Consolidated Statement of Financial Position at \$5.557 billion. Total borrowings consist of general debentures, amounts borrowed from the Government of Canada and its agencies, as well as other notes and loans payable by the Province. The total of these amounts is reduced by sinking fund assets for various debentures. The total debt of the Province, net of sinking fund assets, is comprised of \$4.969 billion in debt reflected in the Consolidated Revenue Fund, \$373 million in Newfoundland Municipal Financing Corporation debt, \$130 million in Newfoundland and Labrador Housing Corporation debt, and other miscellaneous debt of \$85 million.

Figure 1 shows the total debt owing as at 31 March 1995 to 1999 as disclosed in the Consolidated Statement of Financial Position. The figure provides a breakdown of Canadian and foreign currency debt.

## Comments on Selected Financial Information

Figure 1

**Consolidated Summary Financial Statements  
Provincial Debt  
Years Ended 31 March  
(\$ Billions)**



### The Province's Borrowing Program

The Department of Finance is responsible for arranging and directing the annual borrowing requirements of the Consolidated Revenue Fund. The provincial budget determines how much capital market borrowing is required for a fiscal year. The Department monitors the capital markets and provides advice on when and where to borrow. For the 1998-99 fiscal year the Province borrowed \$700.0 million compared to the estimated total borrowing requirements of \$655.0 million. In addition, Newfoundland Municipal Financing Corporation, Newfoundland and Labrador Housing Corporation, and other entities included in the Consolidated Summary Financial Statements borrowed \$137.6 million, for total borrowing of \$837.6 million. Figure 2 compares the Province's estimated and actual borrowing requirements for 1998-99.

## Comments on Selected Financial Information

Figure 2

**Consolidated Summary Financial Statements**  
**Borrowing Requirements**  
**Year Ended 31 March 1999**  
**(\$ 000's)**

|                                               | Estimate      | Actual        |
|-----------------------------------------------|---------------|---------------|
| Consolidated Revenue Fund                     |               |               |
| Current Account                               | \$(123,445)   | \$(166,431)   |
| Capital Account                               | 103,432       | 162,590       |
| Debt Redemptions                              | 322,000       | 304,241       |
| Foreign Exchange Losses                       | -             | 30,405        |
| Sinking Fund Contributions                    | 44,052        | 42,489        |
| Retirement of Pension Liabilities             | 279,000       | 196,000       |
| Increase in Temporary Investments             | -             | 105,479       |
| Other                                         | <u>30,000</u> | <u>25,227</u> |
|                                               | 655,039       | 700,000       |
| Newfoundland Municipal Financing Corporation  | -             | 43,000        |
| Newfoundland and Labrador Housing Corporation | -             | 45,095        |
| Health Care Corporation of St. John's         | -             | 44,670        |
| Other                                         | -             | 4,862         |
| Total                                         | \$ 655,039    | \$ 837,627    |

The Province's debt expense for 1998-99 as recorded in the Consolidated Summary Financial Statements is \$1,008.0 million, which consists of \$230.4 million of pension interest expense on the unfunded pension liability and \$777.6 million which relates to the cost of servicing the Province's debt.

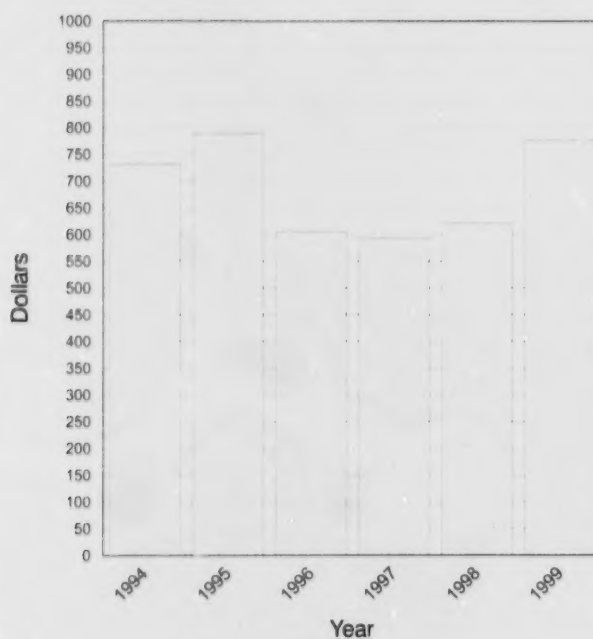
Our review of the Consolidated Summary Financial Statements over the past six years disclosed that the cost of servicing the Province's debt has increased from \$733.1 million in 1994 to \$790.5 million in 1995, then decreased to \$594.0 million in 1997, and increased to \$777.6 million in 1999. This information is contained in Figure 3.



## Comments on Selected Financial Information

Figure 3

**Consolidated Summary Financial Statements**  
**Debt Servicing Costs (Excluding Pension Interest**  
**Expense on the Unfunded Liability)**  
**Years Ended 31 March**  
**(\$ Millions)**



The composition of the cost of servicing the Province's debt for the year ended 31 March 1999 is indicated in Figure 4.

## Comments on Selected Financial Information

Figure 4

### Consolidated Summary Financial Statements Debt Servicing Costs Year Ended 31 March 1999 (\$ Millions)

| Issue                                              | Debt Servicing Cost | Percentage of Total Debt Servicing Cost | Percentage of Debt Portfolio |
|----------------------------------------------------|---------------------|-----------------------------------------|------------------------------|
| Consolidated Revenue Fund                          |                     |                                         |                              |
| Canadian                                           | \$ 226.6            | 22.5%                                   | 27.1%                        |
| CPP / Government of Canada                         | 74.7                | 7.4%                                    | 6.5%                         |
| United States                                      | 197.4               | 19.6%                                   | 18.1%                        |
| Swiss                                              | 83.8                | 8.3%                                    | 4.7%                         |
| Japanese                                           | 11.4                | 1.1%                                    | 0.9%                         |
| Other                                              | <u>102.5</u>        | <u>10.2%</u>                            | <u>6.5%</u>                  |
|                                                    | 696.4               | 69.1%                                   | 63.8%                        |
| Newfoundland Municipal Financing Corporation       | 48.9                | 4.8%                                    | 4.6%                         |
| Newfoundland and Labrador Housing Corporation      | 30.9                | 3.1%                                    | 1.3%                         |
| Other                                              | 1.4                 | 0.1%                                    | 0.9%                         |
|                                                    | 777.6               | 77.1%                                   | 70.6%                        |
| Pension Interest Expense on the Unfunded Liability | 230.4               | 22.9%                                   | 29.4%                        |
| Total                                              | \$1,008.0           | 100.0%                                  | 100.0%                       |

When interest costs on provincial debt exceed any surpluses in revenue over expenditure, Government will have to borrow to cover the shortfall. Additional borrowing causes the total provincial debt to increase and results in even higher interest costs in the following year. This means that Government will have to run even higher surpluses on spending than in the previous year just to cover the growing interest costs for the current period.

As long as Government runs a total budget deficit, that is, when total Government expenditures, including interest, exceed revenues, the



## Comments on Selected Financial Information

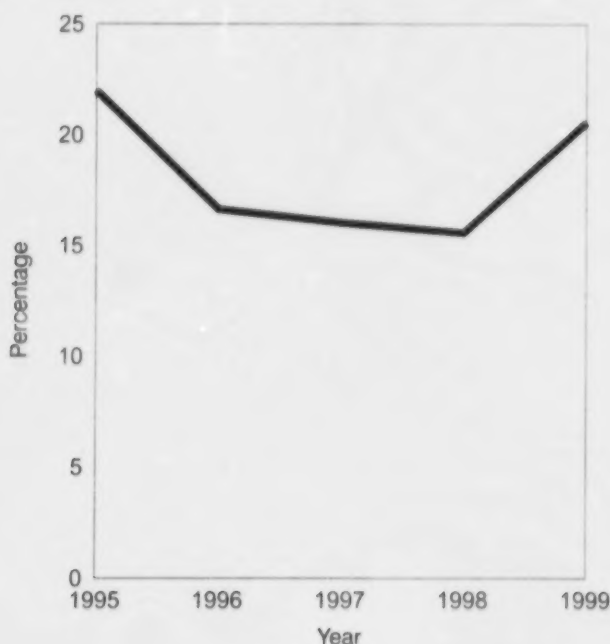
absolute size of the provincial debt will continue to grow causing interest payments to grow. The more Government spends on interest costs the less it has available to spend on Government programs.

Figure 5 indicates that interest costs as a percentage of total revenue decreased for the years 1996 to 1998, and increased for 1999.

**Figure 5**

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**Consolidated Summary Financial Statements**  
**Interest Costs on Borrowings**  
**As a Percentage of Total Revenue**  
**Years Ended 31 March**



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The Province's ability to service its debt relates primarily to both its economy and the magnitude of its debt. Debt as a percentage of gross domestic product (GDP) provides an excellent measure of Government's debt position relative to the Province's economic base. This ratio will increase, and become less favourable, if the total debt grows faster than the provincial GDP. A rise in debt to GDP ratio means that either the burden of the debt on taxpayers is becoming more onerous or that a larger proportion of each tax dollar must be allocated to servicing the debt rather than being spent on Government programs.

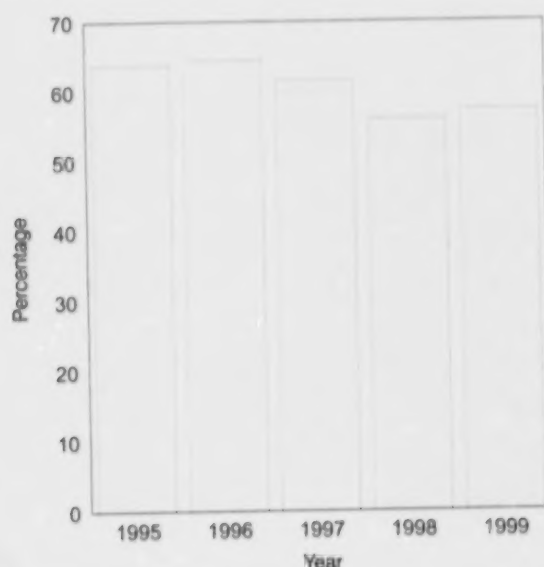
## Comments on Selected Financial Information

Figure 6 shows that borrowings as a percentage of provincial GDP increased slightly from 1995 to 1996, decreased from 1996 to 1998, and then increased slightly for 1999.

**Figure 6**

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**Consolidated Summary Financial Statements  
Borrowings As a Percentage of Provincial GDP  
Years Ended 31 March**



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Our review of borrowings as reported in the Province's Consolidated Summary Financial Statements as at 31 March 1999 indicated that 30% or \$1.973 billion of the debt matures within five years, 23% or \$1.533 billion of the debt matures between six and ten years and 47% or \$3.149 billion of the debt matures in excess of ten years. The composition of this debt maturity profile for the Province is shown in Figure 7.

## Comments on Selected Financial Information

Figure 7

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**Consolidated Summary Financial Statements**  
**Debenture Debt Maturity Profile**  
**31 March 1999**  
**(\$Billions)**



Many of the debentures held by the Province have sinking fund requirements. As well, the Province voluntarily maintains sinking funds for Canada Pension Plan and other debentures. Sinking funds are a pool of cash and investments accumulated during the life of the debentures to repay the debt at maturity. The Province pays the sinking fund contributions to the Board of Trustees of the Newfoundland Consolidated Sinking Funds. This is an unincorporated body appointed by the Lieutenant-Governor in Council. The sinking funds of the Province are administered by the Board of Trustees as one fund known as the Newfoundland Government Sinking Fund. Figure 8 is a summary of sinking funds at 31 March 1999 along with the related debenture debt outstanding and the net amount left after reducing the debt by the amount of the sinking funds.

## Comments on Selected Financial Information

**Figure 8**

**Consolidated Summary Financial Statements**  
**Borrowings and Sinking Funds**  
**31 March 1999**  
**(\$ 000's)**

|                                               | <b>Sinking Fund<br/>Balance</b> | <b>Debt<br/>Outstanding</b> | <b>Balance net of<br/>Sinking Fund</b> |
|-----------------------------------------------|---------------------------------|-----------------------------|----------------------------------------|
| Total Debt With<br>Statutory Sinking<br>Funds | \$ 665,248                      | \$2,972,801                 | \$2,307,553                            |
| Total Debt With<br>Voluntary Sinking<br>Funds | 432,355                         | 1,021,021                   | 588,666                                |
| Total Debt Without<br>Sinking Funds           | -                               | 2,660,743                   | 2,660,743                              |
| <b>Total</b>                                  | <b>\$1,097,603</b>              | <b>\$6,654,565</b>          | <b>\$5,556,962</b>                     |

Figure 9 shows the borrowings net of sinking funds for each of the past five years.

**Figure 9**

**Consolidated Summary Financial Statements**  
**Borrowings and Sinking Funds**  
**Years Ended 31 March**  
**(\$Million's)**

|                 | <b>1995</b>    | <b>1996</b>    | <b>1997</b>    | <b>1998</b>    | <b>1999</b>    |
|-----------------|----------------|----------------|----------------|----------------|----------------|
| Borrowings      | \$6,795        | \$6,725        | 6,291          | \$6,093        | \$6,654        |
| Sinking Funds   | 1,002          | 945            | 985            | 1,042          | 1,097          |
| <b>Net Debt</b> | <b>\$5,793</b> | <b>\$5,780</b> | <b>\$5,306</b> | <b>\$5,051</b> | <b>\$5,557</b> |

## Comments on Selected Financial Information

### 3.5 Foreign Debt

As at 31 March 1999, total borrowings outstanding, as disclosed in the Consolidated Summary Financial Statements, was \$6.654 billion of which \$2.317 billion or 34.8% was repayable in foreign currencies.

Our review of the borrowings as reported in the Province's Consolidated Summary Financial Statements as at 31 March 1995, 1996, 1997, 1998, and 1999 indicated that there was a net increase for 1995 from the previous year of \$346 million. For 1996, 1997 and 1998 there were net decreases from prior years of \$70 million, \$434 million and \$198 million respectively, and for 1999 there was a net increase of \$561 million. The net changes for the five years resulted from the transactions shown in Figure 1.

**Figure 1**

**Consolidated Summary Financial Statements  
Change in Debenture and Other Debt  
Years Ended 31 March  
(\$ Millions)**

|                                                                                   | 1995           | 1996           | 1997           | 1998           | 1999           |
|-----------------------------------------------------------------------------------|----------------|----------------|----------------|----------------|----------------|
| Consolidated Revenue Fund                                                         |                |                |                |                |                |
| Outstanding debenture and other debt, beginning of year                           | \$5,683        | \$6,022        | \$5,939        | \$5,562        | \$5,370        |
| New debt                                                                          |                |                |                |                |                |
| Borrowed                                                                          | 271            | 250            | 100            | 289            | 700            |
| Newfoundland Ocean Enterprises Limited (Assumed)                                  | -              | -              | -              | -              | 71             |
| Newfoundland Farm Products (Assumed)                                              | -              | -              | -              | -              | 10             |
| Pooled Pension Fund                                                               | -              | -              | -              | -              | 6              |
| Other                                                                             | -              | -              | -              | -              | 2              |
| Increase (decrease) in Treasury Bill borrowings                                   | 99             | (3)            | 2              | (35)           | 21             |
| Debt retired                                                                      | (241)          | (146)          | (357)          | (479)          | (346)          |
| Increase (decrease) in debt due to changes<br>in the value of the Canadian dollar | 210            | (184)          | (122)          | 33             | 155            |
| Outstanding debenture and other debt, end of year                                 | 6,022          | 5,939          | 5,562          | 5,370          | 5,989          |
| Newfoundland Municipal Financing Corporation                                      | 605            | 590            | 545            | 474            | 450            |
| Newfoundland and Labrador Housing Corporation                                     | 168            | 169            | 154            | 134            | 130            |
| Other                                                                             | -              | 27             | 30             | 115            | 85             |
| <b>Total</b>                                                                      | <b>\$6,795</b> | <b>\$6,725</b> | <b>\$6,291</b> | <b>\$6,093</b> | <b>\$6,654</b> |

## Comments on Selected Financial Information

The cost of borrowing in foreign currencies is affected by fluctuations in the value of the Canadian dollar. There is a risk that if the value of the Canadian dollar declines in relation to other currencies, the cost of purchasing foreign currencies to pay interest charges or to retire the debt increases. This will result in additional costs to the Province to service the foreign debt.

Figure 2 indicates the exchange rate fluctuations related to the foreign currency debt of the Province.

Figure 2

### Exchange Rates 31 March

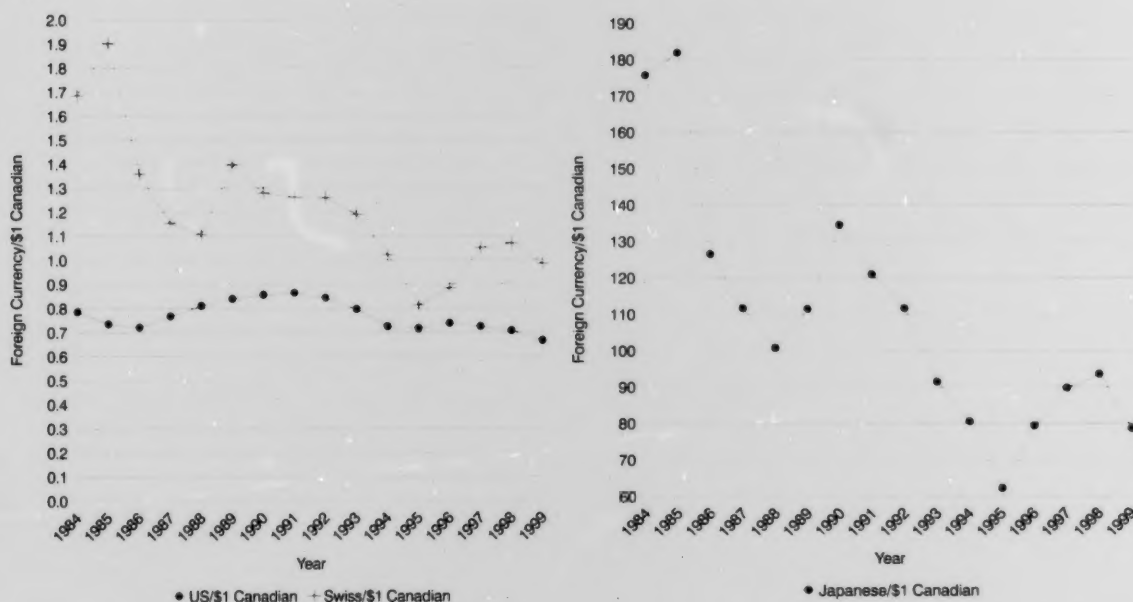


Figure 3 indicates the foreign currency debt issues outstanding as at 31 March 1999. The figure also indicates the interest rate stipulated in the debenture or loan agreement, the Canadian interest rate at the time of issue (as indicated by the Department of Finance) and the effective cost of borrowing for the fiscal years 1994-95 to 1998-99.

## Comments on Selected Financial Information

Figure 3

### Effective Cost of Borrowing Foreign Currency Debt

| Issue                                                                                                                                                                                                                                                                                          | Interest Rate Per Debenture or Loan Agreement | Canadian Interest Rate Available at Time of Issue | Effective Cost of Borrowing * |          |          |          |         |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------|---------------------------------------------------|-------------------------------|----------|----------|----------|---------|
|                                                                                                                                                                                                                                                                                                |                                               |                                                   | 1994-95                       | 1995-96  | 1996-97  | 1997-98  | 1998-99 |
| J6 (Japanese Yen)                                                                                                                                                                                                                                                                              | 5.400%                                        | 10.125%                                           | 17.160%                       | -        | -        | -        | -       |
| J7 (Japanese Yen)                                                                                                                                                                                                                                                                              | 5.400%                                        | 10.125%                                           | 17.160%                       | -        | -        | -        | -       |
| J8 (Japanese Yen)                                                                                                                                                                                                                                                                              | 6.250%                                        | 9.350%                                            | 37.770%                       | (6.630%) | 5.610%   | -        | -       |
| J9 (Japanese Yen)                                                                                                                                                                                                                                                                              | 4.800%                                        | 8.900%                                            | 7.690%                        | (0.290%) | (3.080%) | (2.334%) | 13.478% |
| J10 (Japanese Yen)                                                                                                                                                                                                                                                                             | 4.950%                                        | 8.900%                                            | 6.770%                        | (1.600%) | (1.060%) | (0.674%) | 8.130%  |
| S3 (Swiss Franc)                                                                                                                                                                                                                                                                               | 5.375%                                        | 11.250%                                           | 37.420%                       | 5.050%   | (8.020%) | 9.074%   | 24.341% |
| S4 (Swiss Franc)                                                                                                                                                                                                                                                                               | 5.125%                                        | 11.125%                                           | 21.750%                       | 2.650%   | (5.140%) | 2.671%   | -       |
| S5 (Swiss Franc)                                                                                                                                                                                                                                                                               | 5.000%                                        | 11.000%                                           | 20.810%                       | 4.530%   | (3.670%) | 15.925%  | -       |
| S6 (Swiss Franc)                                                                                                                                                                                                                                                                               | 7.500%                                        | 11.900%                                           | 24.610%                       | 6.750%   | (2.990%) | 6.928%   | 26.867% |
| S7 (Swiss Franc)                                                                                                                                                                                                                                                                               | 7.000%                                        | 11.000%                                           | 25.150%                       | 11.100%  | 1.860%   | 10.295%  | 19.068% |
| S8 (Swiss Franc)                                                                                                                                                                                                                                                                               | 3.250%                                        | 5.700%                                            | -                             | -        | -        | 2.034%   | 6.737%  |
| AE (U.S.S)                                                                                                                                                                                                                                                                                     | 8.500%                                        | 9.750%                                            | 7.180%                        | 4.110%   | 3.030%   | -        | -       |
| AF (U.S.S)                                                                                                                                                                                                                                                                                     | 11.625%                                       | 12.500%                                           | 11.400%                       | 9.530%   | 10.540%  | 11.319%  | 13.743% |
| AG (U.S.S)                                                                                                                                                                                                                                                                                     | 9.000%                                        | 10.100%                                           | 10.330%                       | 9.040%   | 9.990%   | 10.451%  | 12.407% |
| AH (U.S.S)                                                                                                                                                                                                                                                                                     | 9.875%                                        | 11.850%                                           | 12.270%                       | 11.160%  | 12.210%  | 12.898%  | 15.235% |
| AJ (U.S.S)                                                                                                                                                                                                                                                                                     | 10.000%                                       | 11.800%                                           | 12.560%                       | 11.520%  | 12.490%  | 13.211%  | 15.529% |
| AK (U.S.S)                                                                                                                                                                                                                                                                                     | 9.000%                                        | 10.750%                                           | 11.880%                       | 10.480%  | 11.830%  | 12.381%  | 14.957% |
| AL (U.S.S)                                                                                                                                                                                                                                                                                     | 6.050%                                        | 8.640%                                            | -                             | -        | -        | -        | -       |
| AM (U.S.S)                                                                                                                                                                                                                                                                                     | 8.650%                                        | 9.800%                                            | 10.020%                       | 9.300%   | 10.010%  | 10.466%  | 12.365% |
| AN (U.S.S)                                                                                                                                                                                                                                                                                     | 7.320%                                        | 8.500%                                            | 7.810%                        | 7.320%   | 7.680%   | 8.051%   | 9.575%  |
| J11 (U.S.S)                                                                                                                                                                                                                                                                                    | 8.500%                                        | 8.900%                                            | 7.820%                        | 5.390%   | 6.980%   | 8.055%   | 11.934% |
| * The effective cost of borrowing represents the costs of interest, the amortization of foreign exchange gains and losses, and realized exchange gains and losses on sinking fund contributions expressed as a percentage of the Canadian dollars received from the debt at the time of issue. |                                               |                                                   |                               |          |          |          |         |



## Comments on Selected Financial Information

### 3.6 Loan Guarantees

A loan guarantee represents an undertaking by the Province that it will pay the outstanding principal and interest relating to a guaranteed obligation in the event of a default by the borrower. These guarantees may be used to support regional development or to give economic assistance to certain industries or individuals who meet specified criteria. The Province has guaranteed the repayment of principal and interest of certain debentures and bank loans on behalf of municipalities, individuals, and private and Crown corporations.

The responsibility for the issuance of these guarantees rests with the Minister of Finance or such other minister as the Lieutenant-Governor in Council may designate.

These guarantees are not recorded as a direct liability of the Province because they become such only in the event of default. Accordingly, outstanding guarantees are disclosed in a schedule to the Consolidated Revenue Fund Financial Statements. A summary of these guarantees is presented in Figure 1.

Figure 1

**Consolidated Revenue Fund**  
**Loan Guarantees**  
**Years Ended 31 March**  
**(\$ 000's)**

| Description of Guarantee                     | 1998               |            | 1999               |            |
|----------------------------------------------|--------------------|------------|--------------------|------------|
|                                              | Amount             | %          | Amount             | %          |
| <b>Debentures</b>                            |                    |            |                    |            |
| Newfoundland and Labrador Hydro              | \$1,135,010        | 67         | \$1,100,000        | 71         |
| Newfoundland Municipal Financing Corporation | 365,239            | 22         | 372,802            | 24         |
| Municipalities                               | 2,220              | -          | 1,747              | -          |
| Newfoundland Liquor Corporation              | 700                | -          | 500                | -          |
| <b>Bank Loans</b>                            |                    |            |                    |            |
| Crown Corporations                           | 83,036             | 5          | -                  | -          |
| Fisheries                                    | 19,720             | 1          | 20,214             | 1          |
| Municipalities                               | 12,427             | 1          | 2,129              | -          |
| Corporate                                    | 8,353              | -          | 17,974             | 1          |
| <b>Other</b>                                 | 70,169             | 4          | 42,788             | 3          |
| <b>Total</b>                                 | <b>\$1,696,874</b> | <b>100</b> | <b>\$1,558,154</b> | <b>100</b> |



## Comments on Selected Financial Information

The Canadian Institute of Chartered Accountants recommends that loan guarantees be accounted for and reported as contingent liabilities and that a provision for losses on loan guarantees be established when it is determined that a loss is likely. For the year ended 31 March 1999 the Province has established a provision of \$14.4 million for expected losses on loan guarantees, of which \$12.8 million related to Integrated Poultry Limited.

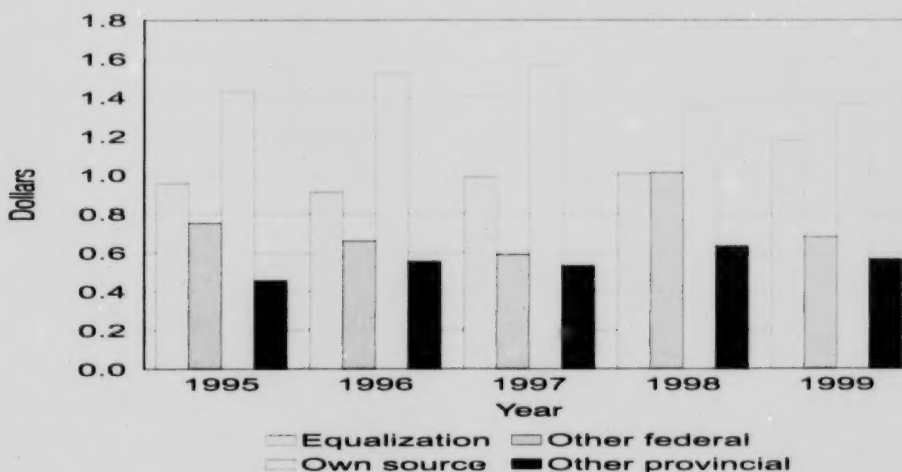
For the period 1 April 1983 to 31 March 1999 the Province has issued corporate loan guarantees totalling \$152.7 million and has been obligated to make payments totalling \$81.1 million on these guarantees. Also, the Province has been obligated to make payments totalling \$3.0 million on fisheries loan guarantees. All of these payouts under guarantee were originally recorded as loans receivable of the Province.

### 3.7 Information on Government's Revenue

Total revenue for the year ended 31 March 1999 was reported in the Consolidated Summary Financial Statements as \$3.785 billion. Figure 1 shows revenue, by source, for the fiscal years to 1995 to 1998.

Figure 1

**Consolidated Summary Financial Statements**  
**Revenue by Source**  
**Years Ended 31 March**  
**(\$ Billions)**



## Comments on Selected Financial Information

The Government of Canada represents the most significant source of revenue for Government, totalling \$1.860 billion in 1999. These revenues include payments received under federal provincial fiscal arrangements relating to Tax Equalization, Canada Health and Social Transfers, cost shared programs, and other payments. Government of Canada revenue represents approximately 49% of all revenues in 1999 (1998 - 50%).

Taxes amounted to \$1.361 billion in 1999. Taxes include Sales Tax, Personal Income Tax, Corporate Income Tax, Gasoline Tax as well as a variety of other taxes. Tax revenues represent approximately 36% of all revenues in 1999 (1998 - 34%).

Aside from the main sources of revenue previously outlined, other sources of revenue exist, totalling \$564 million in 1999. These other revenues relate to miscellaneous revenues such as investment income, vehicle drivers' licences and court fees and forfeitures. Other revenues have decreased from \$632 million in 1998 to \$564 million in 1999. Other revenues represent approximately 15% of total revenue in 1999 (1998 - 16%).

In addition to the above revenue, the Province also received \$348 million in 1997 for Harmonized Sales Tax transitional assistance in respect of anticipated losses in the level of current retail sales tax revenues over the period 1 April 1997 to 31 March 2001. This amount has been deferred and will be recognized as revenue over the periods earned as follows:

|         |               |
|---------|---------------|
| 1997-98 | \$127 million |
| 1998-99 | \$127 million |
| 1999-00 | \$63 million  |
| 2000-01 | \$31 million  |

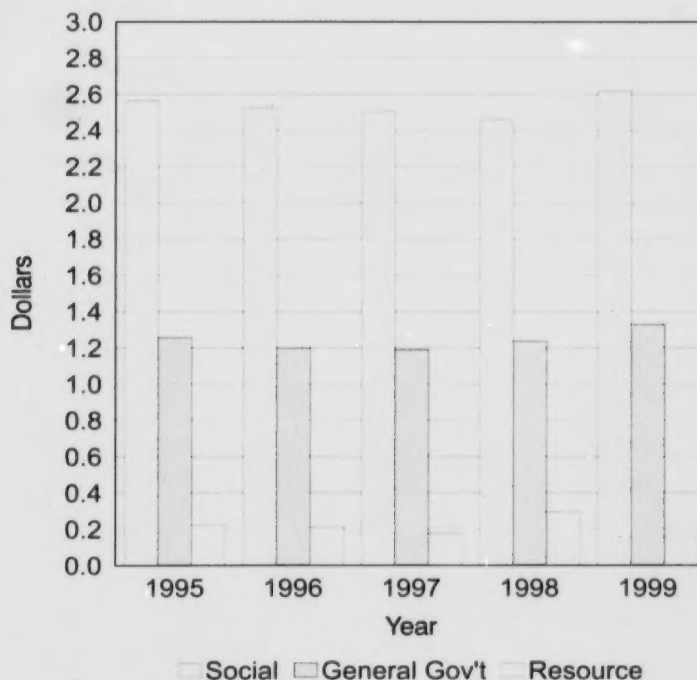
### 3.8 Information on Government's Expenditure

Total expenditure in 1999 was reported in the Consolidated Summary Financial Statements at \$4.105 billion. Figure 1 shows the total expenditure, by sector, for the fiscal years 1995 to 1999.

## Comments on Selected Financial Information

Figure 1

**Consolidated Summary Financial Statements  
Expenditure By Sector  
Years Ended 31 March  
(\$ Billions)**



Social Sector expenditures of \$2.618 billion include the expenditures of the Departments of: Education; Health and Community Services; Justice; Municipal and Provincial Affairs; and Human Resources and Employment.

General Government Sector expenditures of \$1.330 billion include expenditures of: Consolidated Fund Services; Executive Council; the Department of Finance; the Department of Government Services and Lands; Legislature; Public Service Commission; and the Department of Works, Services and Transportation.

Resource Sector expenditures of \$157 million include the expenditures of the Departments of: Development and Rural Renewal; Environment and Labour; Fisheries and Aquaculture; Forest Resources and Agrifoods; Industry, Trade and Technology; Mines and Energy; and Tourism, Culture and Recreation.

## Comments on Selected Financial Information

### 3.9 Contingency Reserve Fund

In its 1996 Budget Speech, Government announced the establishment of a Contingency Reserve Fund of \$30 million. This fund was to be used in case of unforeseen expenditures or where the Province's revenues fall below those projected. In each of its Budgets for the past three years Government has included a Contingency Reserve Fund in the amount of \$30 million. Section 4(4) of the *Supply Act, 1998*, Section 4(2) of the *Supply Act, 1997* and Section 4(2) of the *Supply Act, 1996*, provide that the Lieutenant-Governor in Council may, where an expenditure has not been foreseen and not provided for by the Legislature, transfer sums voted in Contingency Reserve to another Head of Expenditure. During the three years ended 31 March 1999 Government transferred a total of \$88.8 million from the Contingency Reserve Fund to the departments, as shown in Figure 1.

Figure 1 also provides details of the various projects which were funded by Government from the Contingency Reserve Fund for each of the past three years.

## Comments on Selected Financial Information

Figure 1

### Contingency Reserve Expenditures By Department and Project Years ended 31 March

| Department                    | Project                                                                                                  | 1997        | 1998         | 1999        | Total        |
|-------------------------------|----------------------------------------------------------------------------------------------------------|-------------|--------------|-------------|--------------|
| Health and Community Services | The Provinces' share of restructuring the National Blood Supply Program                                  |             |              | \$7,400,000 |              |
|                               | Operating deficits and new funding requirements of institutions                                          |             | \$23,600,000 |             |              |
|                               | Settlement of claims from construction of health care centers in Burgeo, Port Saunders and St. Lawrence. | \$1,903,448 |              |             | \$32,903,448 |
| Education                     | Provincial College Operations \$1.2 million and Student Loans Programs \$5.0 million                     |             |              | 6,200,000   |              |
|                               | Newfoundland and Labrador Education Investment Corporation                                               |             | 1,700,000    |             |              |
|                               | School Board Debt                                                                                        | 15,000,000  |              |             | 22,900,000   |
| Justice                       | Civil Law- Allowances and Assistance - Murray Premises settlement                                        |             |              | 4,200,000   |              |
|                               | Settlement of Petten/Eastern Shipbuilders Case                                                           |             |              | 1,800,000   |              |
|                               | Breathalyzer Units                                                                                       |             |              | 240,000     |              |
|                               | Reclassification of Youth Care Workers                                                                   |             |              | 580,000     |              |
|                               | Settlement of the claim of William Earle                                                                 | 102,300     |              |             |              |
|                               | Settlement for 43 Mount Cashel Claimants                                                                 | 11,238,000  |              |             |              |
|                               | Negotiations relating to the Terra Nova Project, etc.                                                    | 600,000     |              |             | 18,760,300   |

## Comments on Selected Financial Information

Figure 1 (Cont'd)

| Department                         | Project                                                           | 1997         | 1998         | 1999         | Total        |
|------------------------------------|-------------------------------------------------------------------|--------------|--------------|--------------|--------------|
| Municipal and Provincial Affairs   | Fire Commissioner's Office                                        |              |              | 216,400      |              |
|                                    | Special Employment Initiatives                                    |              | 1,000,000    | 3,000,000    | 4,216,400    |
| Forest Resources and Agrifoods     | Special Employment Initiatives                                    |              | 2,500,000    | 1,000,000    | 3,500,000    |
| Human Resources and Employment     | Special Employment Initiatives                                    |              | 300,000      |              |              |
|                                    | Employment Development Programs                                   |              |              | 3,000,000    | 3,300,000    |
| Works, Services and Transportation | Special Employment Initiatives                                    |              | 700,000      | 500,000      | 1,200,000    |
| Tourism, Culture and Recreation    | Tourism miscellaneous grants                                      |              |              | 150,000      |              |
|                                    | Recreation - Operations expenditures                              |              |              | 390,000      |              |
|                                    | Park Vehicles                                                     |              |              | 100,000      |              |
|                                    | Grant to the Johnson Family Foundation - Grand Concourse          | 100,000      |              |              | 740,000      |
| Executive Council                  | Strategic Social Plan                                             |              |              | 500,000      | 500,000      |
| Government Services and Lands      | Permitting and Inspection Services                                |              |              | 108,200      |              |
|                                    | Firearms Legislation Project                                      |              | 200,000      |              | 308,200      |
| Legislature                        | House of Assembly Operations                                      |              |              | 250,000      | 250,000      |
| Development and Rural Renewal      | Initiatives for development and upgrade of the former CN rail bed |              |              | 175,000      | 175,000      |
| Mines and Energy                   | Negotiations relating to the Terra Nova Project, etc.             | 75,000       |              |              | 75,000       |
| Total                              |                                                                   | \$29,018,748 | \$30,000,000 | \$29,809,600 | \$88,828,348 |

Source: Government's accounting records

## Comments on Selected Financial Information

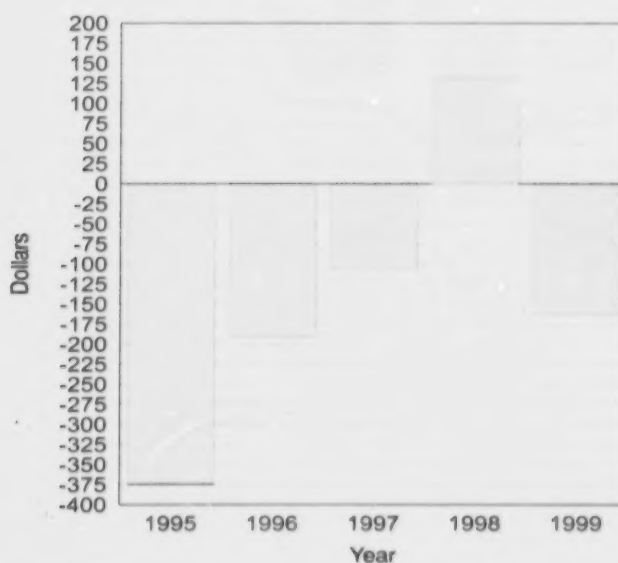
### 3.10 Information on Government's Deficits

In discussing Government's deficits, it is important to differentiate between the Government's deficit in any particular year and the Government's accumulated deficit. The total deficit for the 1998-99 fiscal year, after giving effect to \$157 million (1997-98 - \$129 million) of net income of Government enterprises, was reported in the Consolidated Summary Financial Statements at \$163 million (1997-98 - \$133 million surplus). The total deficit represents the excess of expenditure over revenue for current and capital accounts. The accumulated deficit as at 31 March 1999 was \$7.6 billion (1998 - \$7.3 billion).

Figure 1 shows the deficits (current and capital) of the Province for the years ended 31 March 1995 to 1997, the surplus for the year ended 31 March 1998, and the deficit for the year ended 31 March 1999. As the figure indicates, the Province realized a deficit in four of the last five years. A contributing factor in the surplus in 1997-98 was the receipt of a one-time payment of \$347.6 million from the Federal Government in consideration for the Province assuming all responsibility for operation of the marine, freight and passenger services on and to the coast of Labrador.

**Figure 1**

**Consolidated Summary Financial Statements**  
**Surplus (Deficit) (Current and Capital)**  
**Years Ended 31 March**  
**(\$ Millions)**





## Comments on Selected Financial Information

### 3.11 Service Organization Report

Government uses xwave solutions (formerly NewTel Information Solutions Limited) as its service organization for the electronic processing and storage of data, maintaining and updating programs, and generation of reports. The *Canadian Institute of Chartered Accountants (CICA) Handbook* provides guidance to the auditor of an entity in obtaining audit evidence when the entity uses a service organization.

Since we are required to obtain a sufficient understanding of internal control to plan and conduct the audit of the Public Accounts of the Province, we have to determine the amount of reliance that can be placed on the management and accounting systems in operation. We must also consider the nature and extent of the services provided by xwave solutions including the authority delegated to it and the sufficiency and appropriateness of evidence available from the Province. An important source of this assurance is an opinion on control procedures at the service organization, as outlined in section 5900 of the *CICA Handbook*.

We received a report on control procedures at NewTel Information Solutions Limited in June 1998. It indicated that control objectives reviewed were sufficient to meet the stated objectives of the system, the control procedures described in the report were suitably designed to provide reasonable, but not absolute assurance that the control objectives were achieved, and that control procedures at the data centre operated effectively from 9 February 1998 to 20 February 1998.





**PROVINCE OF NEWFOUNDLAND**

**REPORT OF THE AUDITOR GENERAL**

**TO THE HOUSE OF ASSEMBLY**

**ON REVIEWS OF**

**DEPARTMENTS AND CROWN AGENCIES**

**for the**

**YEAR ENDED**

**31 MARCH 1999**

**PRINTED UNDER THE AUTHORITY OF THE HOUSE OF ASSEMBLY  
ST. JOHN'S, NEWFOUNDLAND**



PROVINCE OF NEWFOUNDLAND

Office of the Auditor General

31 January 2000

The Honourable Lloyd Snow, M.H.A.  
Speaker  
House of Assembly

Dear Sir:

In compliance with the *Auditor General Act*, I have the honour to submit herewith, for transmission to the House of Assembly, my Report on Reviews of Departments and Crown Agencies for the year ended 31 March 1999.

Respectfully submitted,

*Elizabeth Marshall*

**ELIZABETH MARSHALL, C.A.**  
**Auditor General**



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## CHAPTER

I

## AUTHOR GENERAL'S OVERVIEW





CHAPTER  
1  
Auditor General's  
Overview

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## **Auditor General's Overview**

### **1.1 Introduction**

This Report has been prepared in compliance with the requirements of section 12 of the *Auditor General Act*. Section 12 requires that this Report outline significant matters identified during the course of examining the accounts of the Province, agencies of the Crown and other entities which, in the opinion of the Auditor General, should be brought to the attention of the House of Assembly.

In accordance with this provision of the *Act*, this Report includes those instances that have been observed in the course of the audits and additional examinations of departments, agencies of the Crown and other entities, that are considered to be significant. An examination of each of these matters was performed in accordance with generally accepted auditing standards and, accordingly, included such tests and other procedures considered necessary in the circumstances. The instances reported should not be used as a basis for drawing conclusions as to compliance or non-compliance with respect to matters not reported.

Comments on the audit of the financial statements of the Province are contained in a separate report entitled *Report of the Auditor General to the House of Assembly on the Audit of the Financial Statements of the Province for the Year Ended 31 March 1999*. That Report is also submitted to the Speaker of the House of Assembly to be tabled before the House.

### **1.2 Format of the Report**

This Report contains five chapters and four appendices. A brief description of the contents of each chapter follows.

#### **Chapter 1 Auditor General's Overview**

This chapter provides an introduction to the Report and summarizes significant matters which are presented in more detail in other parts of this Report.

#### **Chapter 2 Comments on Public Sector Accountability**

This chapter contains comments and a recommendation relating to the systems of accountability within Government, its departments, agencies of the Crown, and Memorial University of Newfoundland.

#### **Chapter 3 Comments on Audits and Additional Examinations**

The comments in this chapter pertain to the audit observations and recommendations resulting from audits of specific departments and agencies of the Crown. The departmental audits are listed in Appendix II, the financial statement audits performed by the Auditor General are listed in Appendix III, and the financial statement audits performed by private

## **Auditor General's Overview**

sector auditors are listed in Appendix IV. Additional examinations are conducted on a cyclical basis on all Government departments and agencies of the Crown.

### **Chapter 4 Update on Prior Years' Report Items**

This chapter provides an update on action taken with respect to recommendations made in our 1997 and prior Reports.

### **Chapter 5 General Matters and Work of the Audit Office**

This chapter addresses a number of general matters relating to the operations of the Office of the Auditor General including performance objectives and results to date, the audited financial statements of the Office, any special reports issued during the year, and comments relating to the professional activities of the Office.

## **1.3 Highlights**

### **1. 1998-99 Deficit**

The audited financial statements of Government, which are called the Consolidated Summary Financial Statements, indicate that Government (including its 18 departments and the Legislature, its 12 health care boards, its 10 school boards and its 42 Crown agencies) reported a deficit of \$163 million for 1998-99. This deficit and these Financial Statements are the most complete financial information available for Government.

However, Government has traditionally reported the "cash surplus" or "cash deficit" of its 18 departments and the Legislature as its surplus or deficit. This "cash surplus" or "cash deficit" does not include the deficits or surpluses of the 12 health care boards, the 10 school boards or the 42 Crown agencies. In addition, the "cash surplus" or "cash deficit" does not include certain expenditures such as foreign exchange losses and pension-related expenditures. This is consistent with how the budget is prepared. As of 31 March 1999, this "cash surplus" was \$10 million, compared to the \$10 million "cash deficit" which was forecasted in the budget.

In order to have complete information on the Province's finances, I encourage members of the House of Assembly and other interested parties to refer to the Consolidated Summary Financial Statements when discussing the Province's financial position and operating results. I also continue to recommend to government that it prepare its budget on the same basis as the Consolidated Summary Financial Statements so that the Province's budget and Consolidated Summary Financial Statements are comparable.

## Auditor General's Overview

### 2. Special Warrants

Most Government funding is provided by supply acts as a result of the Budget which is debated in the House of Assembly before it is approved by the House of Assembly. However, through the use of special warrants, Government can spend public money without the prior approval of the House of Assembly. All special warrants issued must subsequently be tabled in the House of Assembly and approved.

During 1998-99, Government issued \$136 million in special warrants, most of which were issued in March 1999, the last month of the fiscal year. I have two concerns regarding the issuance of special warrants:

- Special warrants must be issued in accordance with the requirements of the *Financial Administration Act*. In my opinion, \$95 million of the \$136 million of special warrants issued did not comply with the requirements of the *Act* which specifies that the expenditures authorized by special warrant must be urgent.
- The issuance of special warrants impacts the Province's "bottom line" in that particular year. Since expenditures increase as a result of the special warrants, the Province's reported cash position decreases and the deficit of the Consolidated Revenue Fund increases. Specifically:
  - As of 31 March 1999, Government's cash surplus decreased from \$146 million to \$10 million after the issuance of \$136 million in special warrants; and
  - As of 31 March 1999, the deficit, as reported in the audited financial statements of the Consolidated Revenue Fund, increased from \$42 million to \$178 million after the issuance of \$136 million in special warrants.

I am recommending that special warrants be issued only in situations where the expenditure is truly required on an urgent basis.

Further comments on this matter are included in Item 3.4 of this Report.

One special warrant in particular indicated a serious breakdown in controls within Government. On 22 March 1999, Government announced the establishment of the Newfoundland and Labrador Legacy Nature Trust. My review indicated that Government issued a cheque for \$1 million on an urgent basis on the last date of the fiscal year (31 March 1999) to the Newfoundland and Labrador Legacy Nature Trust although, at that point in time, the Corporation did not exist. The cheque was held by

## **Auditor General's Overview**

Government officials for 43 days until it was deposited on 13 May 1999 in a bank account used for bid deposits which accompany public tenders, a purpose entirely unrelated to the nature of the cheque. The Newfoundland and Labrador Legacy Nature Trust was not incorporated until 14 September 1999, 5 months after the cheque was issued on an urgent basis. Further comments on this matter are included in Item 3.24 of this Report.

### **3. Framework of Accountability**

In my previous reports to the House of Assembly, I expressed concern over the lack of information being provided to the House of Assembly by Government departments, agencies of the Crown and the University, which are funded primarily by the public purse. While considerable attention is given to the government's budget which is approved by the House of Assembly, there is little information provided to the House of Assembly on how departments, agencies of the Crown and the University actually spent the money and what this money has actually achieved.

My review of reports tabled in the House of Assembly between 1995 and 1999 has disclosed that no Government department filed an annual report on its operations during that period. In addition, of the 63 entities receiving Government operating grants totaling \$1.9 billion in 1997-98, only 5 entities receiving \$164 million had their reports tabled in the House of Assembly. I do not anticipate any improvements in the number of reports tabled in 2000 for the 1998-99 fiscal year.

In 1997 I was informed that Government was proceeding with the implementation of a new accountability framework for Government departments. During that same year, Government established a Task Force to focus on the development of an accountability framework for Crown agencies. Although Government is continuing with these initiatives, I am concerned about the lack of progress being made. For example, there is still no legislation establishing an accountability framework for government departments, agencies of the Crown and the University, and there is still no requirement that annual reports be prepared and tabled in the House of Assembly.

Further comments on this matter are included in Item 2.1 of this Report.

### **4. Health Care Boards**

During 1999 I continued my review of the Province's eight hospital boards and four community health care boards. Of the \$3.8 billion in government expenditures in 1998-99, grants and subsidies paid to the eight hospital boards amounted to \$700 million or 16.8% of government expenditures, while the four community health care boards received \$133 million.



## Auditor General's Overview

The financial position of the hospital boards and community health care boards continues to deteriorate. Included in the \$700 million paid to the hospital boards and the \$133 million to the community health care boards in 1998-99 was additional funding of \$48.4 million and \$2.3 million respectively to the approved budgets. The Province has also approved additional funding of \$18.7 million to the hospital boards and \$4 million to the community health care boards for 1999-2000. As of December 1999, the hospital boards and the community health care boards were projecting deficits of \$30.6 million and \$7.8 million respectively before non-shareable expenditures such as severance and vacation pay for the 1999-2000 fiscal year.

As of November 1999, which was eight months into the 1999-2000 fiscal year, the Department of Health and Community Services had yet to finalize the 1999-2000 budgets of its hospital boards and community health care boards. A board's budget reflects its operational plan for the year and is based on assumptions that certain programs and services will be provided at certain levels. The board's budget should be finalized by Government before each fiscal year and if this is not possible it should be finalized very early in the new fiscal year. The budget supports the board's planned operational activities for a particular year and also indicates Government's agreement with the programs and services reflected in the budget. In addition, it confirms the level of funding which will be provided by Government. As a result, Government finalization of the board's budget is important.

Further comments on this matter are included in Items 3.29 and 3.30 of this Report.

In addition to assessing the financial position of the hospital boards and the community health care boards, I completed a review of two hospital boards as follows:

- A financial review of the Peninsulas Health Care Corporation was undertaken in 1999. This Corporation, similar to other health care boards in the Province, has incurred deficits over the past several years. While additional funding has been provided by Government, the Corporation, at the time of our review, estimated that it will incur a deficit of \$6.1 million in 1999-2000. Subsequent to our review, Government approved additional funding of \$1.0 million.

Details of my review are included in Item 3.28 of this Report.

## Auditor General's Overview

- My audit of the Western Memorial Hospital Corporation in 1996 identified significant problems in the financial operations of the Corporation. My follow-up audit in 1999 indicated that the Corporation has made improvements in its financial management. There are some areas that require further attention and these have been included in my Report to management.

One of the major issues facing the Corporation is its poor financial position. While Government has provided additional funding of \$20.9 million in 1998-99, there remains a deficit of \$19.4 million as of 31 March 1999 which will have to be funded some time in the future by Government or through savings by the Corporation. In addition, at the time of our review in 1999, the Corporation was forecasting an additional deficit of \$15.7 million in 1999-2000. Subsequent to our review, Government approved additional funding of \$4.98 million.

The Corporation, since my initial review in 1996, has been the subject of several additional reviews undertaken at the initiative of Government. As part of my follow-up audit in 1999, I requested copies of two specific reviews - the Atkinson Report which was completed in 1999 at a cost of \$242,000 and an internal review undertaken by the Department of Health and Community Services in 1998-99. I was informed by the Department of Health and Community Services that neither report could be provided to me as they were before Cabinet and therefore, under Section 19 of the *Auditor General Act*, were not required to be provided to me. As a result, my detailed Report does not include a reference to either of the reviews.

Details of my review are included in Item 3.27 of this Report.

### 5. Municipal Debt

Prior to 1997, most municipal debt was financed by Government through the Newfoundland Municipal Financing Corporation (NMFC) and as a result, information on most municipal debt was readily available through the accounting records of NMFC. In 1997, many municipalities began to refinance their NMFC debt through chartered banks and as a result, it became more difficult to determine the amount of municipal debt.

The database of information maintained by the Department of Municipal and Provincial Affairs, which should indicate the amount of municipal debt, was inaccurate and incomplete at the time of our review. As a result, the Department could not provide us with the total amount of municipal debt outstanding as of 31 December 1998, which was the most recent year end for which information should be available. Given the concerns



## Auditor General's Overview

identified in recent years over the financial condition of the municipalities, the extent of the debt, and their ability or inability to service their debt, the Department of Municipal and Provincial Affairs should know the debt load of municipalities, both individually and in total.

Although the amount of municipal debt financed through the Newfoundland Municipal Financing Corporation is decreasing (it decreased from \$445 million as at 31 December 1994 to \$330 million as at 31 December 1998), payments in arrears are increasing. For example, arrears were \$10.8 million as of 31 December 1993, while the arrears as of 31 December 1998 had increased to \$19.2 million. Complete information on bank debt and related payment arrears was not available in the Department.

Details of my review are included in Item 3.34 of this Report.

### **6. Strategic Enterprise Development Fund (ENL)**

ENL was created in 1991 as an amalgamation of the former Newfoundland and Labrador Development Corporation and divisions of the former Department of Development. In 1996 the operations of ENL were transferred to the Department of Development and Rural Renewal. ENL provides capital financing to assist the start up and growth of small and medium size businesses.

I have three major concerns regarding the operations of ENL:

- ENL has never reported publicly on its operations and performance. Such a report would provide details on the individual businesses assisted, the economic benefits created by these businesses, the number of jobs actually created, the cost per job, and how much the Corporation collects compared to what it should have collected. Such information should be generated, audited, and tabled in the House of Assembly. Without accurate information on its performance, the Corporation, Government, and the House of Assembly does not know how the Corporation is performing.

Information required for performance reporting goes beyond traditional financial information that is currently lacking at the Corporation. As a result, the Corporation faces significant challenges in generating accurate performance information.

## Auditor General's Overview

- Financial systems at the Corporation do not provide the financial information required to properly manage the loan and equity portfolio. While some information is available, other essential information (such as the rate of recovery of principal and interest owing to the Corporation) is very difficult to obtain.
- Financial statements of ENL are not prepared and available for audit on a timely basis. For example, Government requires that all financial statement audits for Crown agencies be completed by 30 June of each year. For the year ended 31 March 1999, the financial statements of ENL were not presented for audit until August 1999.

In addition to the above, we also reviewed the procedures used by the Corporation in assessing and evaluating proposals for funding and the manner in which the Corporation is monitoring its loan and equity portfolio. My review identified weaknesses in the assessment and evaluation of proposals and the monitoring of its accounts. Therefore, I am recommending that these areas be reviewed and appropriate action taken.

Details of my review are included in Item 3.10 of this Report.

### **7. Strategic Enterprise Development Special Reserve Fund**

In March 1997 Government transferred \$10 million to the Strategic Enterprise Development Fund which was intended to be used to strengthen the small to medium sized business development efforts of the Department of Development and Rural Renewal. An additional \$1.975 million was provided in the 1998-99 fiscal year. The \$11.975 million fund was referred to as the "Special Reserve Fund".

We reviewed three projects which received funding of \$11.3 million from the Special Reserve Fund. Our review indicated that these three projects were not subject to the same policies and procedures which applied to other projects in that thorough assessments of these projects were not carried out and verification of business plan assertions was limited. For example, in all three cases, several major issues were identified by government officials but were not resolved, even though the projects were funded. In addition, it was evident from our review that these projects were "pre-approved" before they were approved by the Board of Directors of Enterprise Newfoundland and Labrador Corporation, which was the funding agency.

Further comments on these three projects are included in Item 3.11 of this Report.

## Auditor General's Overview

### 8. Newfoundland Farm Products Corporation

During the year I reviewed the extent of financial and other assistance provided by Government to Integrated Poultry Limited since 1997 when it assumed the operations of the Crown corporation, Newfoundland Farm Products Corporation. A summary of the more significant terms of the purchase and sale agreement between Newfoundland Farm Products Corporation and Integrated Poultry Limited was provided in my 1998 Report to the House of Assembly.

The most significant Government assistance provided to Integrated Poultry Limited has been \$8.5 million in operating and capital grants (\$4.5 million for operations and \$4.0 million for capital infrastructure), a leasehold interest in land and buildings in St. John's, machinery and equipment, and government guarantees which had a current obligation at December 1999 of \$12.5 million. In December 1999, Government was called upon to honour the guarantee and on 16 December 1999 paid \$11.5 million in relation to its obligation. Government elected to require the bank to realize upon its security and to notify Government of the amount of any deficiency up to the remaining \$1.0 million guarantee obligation.

Over the ten year period from 1987-88 to 1996-97, the Province provided operating subsidies totalling \$36 million or, on average, \$3.6 million annually to Newfoundland Farm Products Corporation. In January 1999, Government also assumed the demand loan of \$10.2 million of Newfoundland Farm Products Corporation and this \$10.2 million is now recorded as a direct debt of the Province. In addition, interest for the period April 1998 to February 1999 totalling \$624,000 was reimbursed by Government to Newfoundland Farm Products Corporation.

Details of my review are included in Item 3.25 of this Report

### 9. Newfoundland Government Fund Limited

The Newfoundland Government Fund Limited is a Government administered venture capital fund under the *Immigration Act* (Canada) and Regulations. At the time of my review in October 1999, the Corporation had not complied with the *Immigration Act* (Canada) or the Confidential Offering Memorandum. For example, my most significant concern was that, contrary to the *Act*, the Corporation had not invested any of the required 70% of the \$13.5 million investment proceeds (\$9.45 million) in eligible business operations within nine months of the release of the proceeds from the escrow agent.

## **Auditor General's Overview**

While the Corporation did approve the use of investor funds in 1998 for the construction of the Harbour Breton hospital and advanced approximately \$1.6 million for this project, it was subsequently cancelled and the \$1.6 million was refunded to the Corporation.

Details of my review are included in Item 3.32 of this Report.

### **10. Aquaculture Program**

Last year I reported on the Province's financial exposure through a loan guarantee issued to an aquaculture licensee which had increased to \$6.7 million by September 1998. I now report that Government's involvement with this company is estimated to have cost \$9.3 million in loans and loan guarantees as of 31 March 1999. The \$9.3 million is comprised of a \$6.5 million loan guarantee balance which the Province was called upon to honor and a \$2.8 million loan with Enterprise Newfoundland and Labrador Corporation, which the Corporation has considered to be uncollectible.

Despite the infusion of \$9.3 million by Government, the company's financial position has deteriorated significantly. It is unlikely that Government will recover any of the \$9.3 million in financial assistance provided to the company.

Details of my review are included in Item 3.23 of this Report.

### **11. The Canada-Newfoundland Economic Renewal Agreement**

The Canada-Newfoundland Economic Renewal Agreement is a cost-shared agreement between the Federal and Provincial governments and covers the period 1 April 1996 to 31 March 2001. Funding under the Agreement totals \$100 million, of which \$80 million is provided by the Federal Government and \$20 million by the Provincial Government. As of 31 March 1999, \$51 million in project funding had been provided to third party individuals and organizations.

Our review indicated that the programs and related projects are, for the most part, being properly implemented, monitored and managed. Some issues were identified which have been brought to the attention of Government, the most significant of which was the lack of inspection or audit of individuals and organizations receiving funding under the Agreement. Discussions with Government officials indicate that issues identified during our review are being addressed.

## **Auditor General's Overview**

Our review of this Agreement indicated significant improvements as compared to the Canada-Newfoundland Strategic Investment and Industrial Development Cooperation Agreement on which I reported in my 1996 Annual Report to the House of Assembly.

Details of my review are included in Item 3.3 of this Report.

### **12. Cellular Phones in Government**

The number of cellular phones in government is increasing. As a result, we reviewed the controls over the acquisition and administration of cellular phones in Government in 1999 to determine whether they were adequate.

Standard desk telephones in government are governed by policies that are designed to control their acquisition and installation. These telephones are controlled by serial number and telephone number. In addition, responsibility for the acquisition and installation of telephones and the maintenance of inventory resides in the Department of Works, Services and Transportation. No such policies exist for cellular phones.

While some Departments have formulated policies for the acquisition and administration of cellular phones, others have not. However, generally speaking, policies governing cellular phones are not as structured as those established for standard desk telephones. As a result, I am recommending that Government establish a government-wide policy to control the acquisition and administration of cellular phones.

Details of my review are included in Item 3.5 of this Report.

### **13. A Review of the Financial Management System**

The replacement of Government's financial management system in 1998-99 was a significant undertaking which involved over 15 departments and 500 users at 31 different locations. I am pleased to report that my review indicated that the system was implemented successfully within time and within budget. I commend Government for this achievement.

Details of my review are included in Item 3.8 of this Report.

### **14. Management of Crown Lands**

The Department of Government Services and Lands is responsible for the management of the Province's Crown lands. During the year I reviewed the Department's policies and procedures as they relate to the management of Crown lands. My review indicated the following:



## Auditor General's Overview

- The Department does not have a comprehensive land use policy to facilitate a co-ordinated approach for land use within the Province. The Department expects to complete its work in this area in 2000.
- There is no comprehensive and complete land parcel identification system for all land within the Province. The Department indicated that a comprehensive land parcel identification system would be very costly and as a result it is updating information on land boundaries on an on-going basis as land claims are settled under the *Lands Act* and the *Quieting of Titles Act*.

Several other areas were reviewed including the processing of applications for Crown land, the sale of Crown lands and the development of cottage lots. In addition, we reviewed the collection of amounts owed to the Department for Crown land transactions, the reported total of which was \$2.7 million as of 31 March 1999.

Details of my review are included in Item 3.26 of this Report.

### 15. Debt Relief Program

During 1996-97, the Department of Municipal and Provincial Affairs introduced a Debt Relief Program to assist municipalities in poor financial condition. As at 31 March 1999, the Newfoundland Municipal Financing Corporation had been provided a total of \$17 million of which \$6.1 million had been allocated to 13 municipalities as at 31 March 1999 leaving an unallocated balance of \$10.9 million. Draft Guidelines relating to the Program indicated that *"the municipalities that will be targeted are those that spend more than 30% of their municipal revenues on debt"*. In addition, it was indicated that the order of priority would be given to municipalities with the highest debt to revenue ratio *"but priority may change to accommodate special circumstances"*. My review indicated a number of issues with the Program as follows:

- Reviews of municipalities were not proceeding as quickly as originally planned.
- Municipalities with the highest debt to revenue ratio were not reviewed on a priority basis.

## **Auditor General's Overview**

- The lack of definitive indicators as to the qualifications that had to be met to receive assistance resulted in a process which was not transparent. For example, many municipalities did not receive funding even though their debt to revenue ratio exceeded the 30% identified in the Guidelines. Many municipalities that did receive funding were left with debt to revenue ratios exceeding 30%. As well, two municipalities received funding although their debt to revenue ratio was less than 30%.

Details of my review are included in Item 3.35 of this Report.

### **1.4 Acknowledgments**

I express my appreciation to the officials of Government departments, agencies of the Crown and other entities for the cooperation and assistance provided to my staff during the performance of our work.

I acknowledge the cooperation and assistance provided to my Office during the year by the officials of the Treasury Board Secretariat and the Department of Finance.

I also extend my appreciation to my staff for their outstanding work and the professional manner in which they have carried out their responsibilities.

CHAPTER

2

COMMENT ON

PUBLIC SECTOR ACCOUNTABILITY





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## **Comments on Public Sector Accountability**

### **2.1 Framework of Accountability**

#### **Introduction**

Full accountability requires that Government, its departments, agencies of the Crown, and Memorial University of Newfoundland (the University) be held accountable to the House of Assembly for their use of public money and the delivery of their programs. In addition to providing annual audited financial statements, full accountability requires that Government and these entities be held accountable for the performance of their specific programs compared with their approved objectives.

In my previous Reports to the House of Assembly, I expressed concern over the lack of information being provided to the House of Assembly by agencies of the Crown and the University which are funded primarily by the public purse. Operating grants paid to hospitals, school boards, other agencies of the Crown and the University by government departments are included in total funding approved for each department by the House of Assembly as part of the annual budgetary process. Having approved this funding, the House of Assembly should then receive information on how this public money was used and what the funding has achieved.

To ensure that Government, its departments, agencies of the Crown and the University are held accountable for their programs and use of public resources, in my previous Reports I have recommended the development of an accountability framework for all public sector entities in the Province. This should include Government, its central agencies, departments, agencies of the Crown and the University. I have recommended that the framework include a strategic and operational planning process, clearly defined objectives, measurement criteria, a financial budget and a reporting system which provides appropriate information at various levels. The reporting process should include a report to the House of Assembly on the financial and performance results of each entity compared with its approved plan.

## Comments on Public Sector Accountability

I am concerned over the lack of information being provided to the House of Assembly. While considerable attention is given to the government's budget, there is a lack of emphasis on receiving and reviewing information on how agencies of the Crown and the University actually spend the monies which were approved during the budgetary process. Figure 1 provides a summary of the 1998 annual reports and financial statements by sector tabled in the House of Assembly.

**Figure 1**

### **Annual Reports and Financial Statements by Sector Tabled in the House of Assembly 1998 Year End**

| <b>Sector</b>                                                         | <b>Number of<br/>Entities</b> | <b>Number of 1998<br/>Annual Reports and<br/>Financial Statements<br/>Tabled</b> | <b>Government<br/>Operating Grants<br/>Paid in 1997-98<br/>(\$ Millions)</b> |
|-----------------------------------------------------------------------|-------------------------------|----------------------------------------------------------------------------------|------------------------------------------------------------------------------|
| Health Care Boards                                                    | 18                            | 0                                                                                | \$615                                                                        |
| School Boards and Related Entities                                    | 11                            | 0                                                                                | 485                                                                          |
| Labrador Transportation Initiatives Fund                              | 1                             | 0                                                                                | 349                                                                          |
| Memorial University of Newfoundland                                   | 1                             | 0                                                                                | 125                                                                          |
| Community Health Boards                                               | 4                             | 0                                                                                | 59                                                                           |
| Colleges                                                              | 4                             | 0                                                                                | 40                                                                           |
| Newfoundland and Labrador Education<br>Investment Corporation         | 1                             | 0                                                                                | 25                                                                           |
| Other Crown Agencies receiving<br>Government Operating Grants         | 23                            | 5                                                                                | 207                                                                          |
| <b>Total Crown Entities Receiving<br/>Government Operating Grants</b> | <b>63</b>                     | <b>5</b>                                                                         | <b>\$1,905</b>                                                               |
| Other Crown Agencies not receiving<br>Government Operating Grants     | 33                            | 6                                                                                | 0                                                                            |
| <b>Total</b>                                                          | <b>96</b>                     | <b>11</b>                                                                        | <b>\$1,905</b>                                                               |



## Comments on Public Sector Accountability

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|-------------------------------------------------------------------|-----------------------|------------------------------------------------------------------------|--------------------------------------------------------------------|
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| School Boards and Related Entities                                | 11                    | 0                                                                      | 485                                                                |
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| Total Crown Entities Receiving<br>Government Operating Grants     | 63                    | 5                                                                      | \$1,905                                                            |
| Other Crown Agencies not receiving<br>Government Operating Grants | 33                    | 6                                                                      | 0                                                                  |
| Total                                                             | 96                    | 11                                                                     | \$1,905                                                            |



## Comments on Public Sector Accountability

Of the 63 entities receiving government operating grants of \$1.905 billion in 1997-98, only 5 entities, receiving \$163.5 million, had their reports tabled in the House of Assembly (See Figure 2). In summary, the House of Assembly received reports on entities which had received \$163.5 million of total operating grants of \$1.905 billion. There were no reports tabled in the House of Assembly which related to the remaining \$1.741 billion.

**Figure 2**

### **Annual Reports and Financial Statements Tabled in the House of Assembly 1998 Year End**

| <b>Entity</b>                                      | <b>Government Operating<br/>Grants Paid in 1997-98<br/>(\$000's)</b> |
|----------------------------------------------------|----------------------------------------------------------------------|
| Newfoundland Medical Care Commission               | \$161,765                                                            |
| C. A. Pippy Park Commission                        | 872                                                                  |
| Operation ONLINE Inc.                              | 424                                                                  |
| Provincial Advisory Council on the Status of Women | 384                                                                  |
| Newfoundland Crop Insurance Agency                 | 52                                                                   |
| <b>Total</b>                                       | <b>\$163,497</b>                                                     |

My review of reports tabled in the House of Assembly between 1995 and 1999 has disclosed that no government department filed an annual report on its operations during that period. In addition, few agencies of the Crown have tabled individual annual reports in the House of Assembly.

For the few annual reports which are tabled in the House of Assembly most do not provide adequate accountability information. Most provide general information on the entity and statistical information on its operations. The reports do not provide information on the strategic plans and objectives of the entity or information on what was actually achieved during the year compared with an approved plan.



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|----------------------------------------------------|----------------------------------------------------------------------|
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## Comments on Public Sector Accountability

In one case, only the audited financial statements of the entity were tabled in the House of Assembly. While financial statements present the financial position and results of operations of the entity for the period covered by the statements, they do not provide information relating to an entity's performance in relation to its approved objectives. Therefore, financial statements are only one part of a complete system of accountability.

### Accountability of Government Departments

Prior to 1989 the various acts which created the departments of Government (with the exception of the Department of Justice) required that the minister report annually to the Lieutenant-Governor in Council on the affairs of the department and that such reports be tabled in the House of Assembly within fifteen days of being submitted to the Lieutenant-Governor in Council. In 1989 the old departmental acts were repealed and new legislation was passed. These new acts did not contain a provision which required the preparation and tabling of an annual report by each department. Therefore, at the present time there is no legislative requirement for each department to prepare and table an annual report in the House of Assembly. As a result, we have now reached the point where no department has tabled an annual report in the House of Assembly within the past five years.

Government has embarked on a process to develop a system which will require that each department prepare an annual business plan, set out performance targets and report on results. In June 1997, the Minister of Finance and President of Treasury Board was directed by Cabinet to proceed with the implementation of a new authority and accountability framework for government departments. As part of this framework, Treasury Board was directed to institute a process of annual business plans which would form an integral part of the system. For the 1997-98 year the Board was directed to establish a formal mechanism to outline program review objectives and other key budgetary planning objectives for departments and to hold departments accountable for attaining results. For the 1998-99 year the Board was directed to implement more formalized departmental business plans as part of the budgetary process.

In October 1998 Cabinet Secretariat issued *Guidelines for Departmental Planning 1999-2000 to 2001-2002*. As part of this planning process, departments were required to set out performance targets and measure results against these targets. In future, departments will be required to prepare an annual progress report outlining progress during the fiscal year. The progress report for the 1998-99 year was to have been completed by 31 May 1999 and to serve as an appendix to the 2000-01 plan. This requirement was subsequently deferred in recognition of the need to provide departments with additional support and training in the

## Comments on Public Sector Accountability

development of performance measurement systems. The guidelines for the departmental plans 1999/2000 - 2001/2002 state that progress reports for the 1999-2000 plan are to be presented by May 31, 2000.

In October 1999 Treasury Board Secretariat issued *Guidelines for the Preparation of the 2000-2001 Estimates and Three-Year-Financial Plan*. The *Guidelines* noted that the budget process builds on budgeting and major review processes of recent years. This will be accomplished by extending the fiscal planning horizon into the next millennium. The document further notes that the 2000-2001 budget process will see an increased emphasis on the "accountability" of executives and management in departments and the various public bodies that report through them and their respective ministers. However, the document also states that "*The Accountability Initiative is in a very early stage. Full implementation will require considerable effort over the next number of years. To date, line departments have identified those components of the accountability framework which apply to each of the public entities reporting to their respective Ministers. For most boards with large financial and administrative infrastructures, full compliance will be expected. As such, the strategic planning and budgeting processes of both departments and their affiliated boards will need to be integrated. It is understood that at this early stage, little if any of this type of comprehensive integration will be reflected in budget submissions by departments.*"

### Accountability of Crown Agencies and Memorial University

I am pleased to report that Government has embarked on a process to hold its agencies of the Crown accountable for their performance. In March 1999, Cabinet directed Treasury Board Secretariat to proceed with implementation of a new accountability framework for all Crown corporations, boards and agencies. This framework is designed to permit Government to integrate planning and monitor performance of these entities. Cabinet also directed that any legislative amendments required to implement the framework be drafted by the Office of the Legislative Council.

On 25 May 1999, Government tabled a Bill in the House of Assembly entitled "An Act to Provide an Accountability Framework for Public Bodies". The House of Assembly adjourned on 14 December 1999 and up to that time this Bill received only first reading. The Bill defines a public body as a school board, a hospital board and a regional health and community services board. It does not apply to government departments, other Crown corporations or the University. The Bill requires that "...where the minister requests ...", a public body shall provide a strategic plan and financial reports. The Bill provides the minister with the authority

## **Comments on Public Sector Accountability**

to make recommendations to or direct a public body on ways to more adequately carry out its mandate. I now understand that Government does not intend to proceed with enactment of the Bill.

In July 1999 Treasury Board directed that the accountability framework initiative proceed to be implemented as policy. Also, in July 1999 Government issued "Achieving Excellence - Accountability Framework Guidebook" to all agencies subject to Government's Accountability Framework. The Guidebook provides direction to all agencies of the Crown relating to planning, monitoring and reporting, and feedback. It is designed as an information source to assist in ensuring that program objectives are set, communicated, measured and achieved.

Treasury Board Secretariat has informed us that it has made progress in the design and implementation of its accountability framework. This progress includes the following:

- Co-ordinators have been appointed to lead the initiative in each department;
- Information sessions, highlighting the importance and requirements of the framework, have been held for department managerial and executive staff and project co-ordinators.
- Sessions have also been held with many of the chairs and CEOs whose boards will be impacted by the framework;
- A handbook of information and materials has been compiled for each minister. In addition, ministers have been asked to review the list of entities reporting to their departments to identify the appropriate level of framework compliance; and
- There are efforts to integrate departmental and agency strategic planning to ensure consistency and continuity of government's overall objectives.

### **The Need for a Legislated Framework of Accountability in this Province**

A fundamental principle of accountability is that an entity cannot be accountable to itself. True accountability requires that entities be held accountable to those who provide the resources for their operations. On behalf of the taxpayers of the Province, the House of Assembly approves the allocation of resources to Government, its departments, agencies of the Crown and the University. True accountability would require that these entities, in turn, report back to the House of Assembly on their use of the

## Comments on Public Sector Accountability

resources granted. If these entities do not provide any information on their use of the resources granted to them, or if they provide information only to Government, then we cannot say that a true system of accountability exists. While we may have a system with some administrative controls, we do not have a system of accountability.

In 1979 the (Canadian) *Royal Commission on Financial Management and Accountability* (Lambert Commission) stated: "*Accountability is the essence of our democratic form of government. It is the liability assumed by all those who exercise authority to account for the manner in which they have fulfilled responsibilities entrusted to them, a liability ultimately to the Canadian people owed by Parliament, by the Government and, thus, every government department and agency.*"

Each year since 1992, in my Annual Reports to the House of Assembly, I have made comments and recommendations respecting the need for a legislated framework of accountability for Government, its departments, agencies of the Crown and the University. I have recommended that an accountability framework be developed and that this framework be supported by legislation. I have noted that other provinces and the Government of Canada have established various systems of accountability which include, as a minimum, the preparation of annual reports in a prescribed format. These jurisdictions have established performance measurement criteria and are now using these to report on their performance relative to their approved plans. I am concerned that while other jurisdictions have developed and are using performance measurement criteria, the problems in this Province are much more basic. We do not even have a requirement for Government, its departments, agencies of the Crown or the University to prepare an annual report and have it tabled in the House of Assembly. While Government has commenced implementation of an accountability framework there is still no legislation requiring that these entities prepare annual reports for tabling in the House of Assembly.

It is indeed unfortunate that this is the only province in Canada where no departments and very few agencies of the Crown prepare and publish annual reports and have them tabled in the House of Assembly. While other jurisdictions have been developing and implementing ways to modernize and improve their performance reporting, as far as reporting information to the House of Assembly is concerned, this Province is now further behind than it was in the 1980's and early 1990's. At least during that period some departments were preparing and tabling some form of annual report in the House of Assembly. In my opinion the only way that this situation will ever be resolved is through legislation which specifically requires that Government, its departments, agencies of the Crown and the University prepare and publish annual reports and have them tabled in the House of Assembly.



## Comments on Public Sector Accountability

### Conclusion

While I am pleased to see that some action has been taken, I am concerned that Government has not introduced legislation designed to hold its departments, agencies of the Crown and the University accountable to the House of Assembly for their performance and use of public resources. The Bill which is presently before the House of Assembly is designed to hold only those entities which are defined as public bodies (ie. hospital boards, school boards, and regional health and community services boards) accountable for their operations, and then only if the minister requests. However, as noted above, I now understand that Government has decided not to proceed with enactment of this legislation.

My review of the Hansard of the House of Assembly has disclosed that of the \$1.905 billion paid to 63 Crown entities for government operating grants for the 1997-98 year, the House of Assembly received reports on only 5 entities which had received \$163.5 million.

While Government has made some progress toward the development and design of a framework of accountability, no annual reports have been provided to the House of Assembly by Government or its departments. There is no legislation requiring Government, its departments, agencies of the Crown and the University to be accountable to the House of Assembly for their operations and use of public resources. On behalf of the taxpayers of the Province, the House of Assembly approves the allocation of resources to Government, its departments, agencies of the Crown and the University. True accountability would require that these entities, in turn, report back to the House of Assembly on their use of the resources granted. If these entities do not provide any information on their use of the resources granted to them, or if they provide information only to Government, then we cannot say that a true system of accountability exists.

Government should complete its work in establishing a framework of accountability. This framework should apply to all departments, agencies of the Crown and Memorial University of Newfoundland. If this framework is to be successful it is imperative that it be approved by the House of Assembly and enacted in legislation and that it specifically require the tabling of annual reports in the House of Assembly.

### Recommendation

*Government should complete its work in establishing a framework of accountability for all public sector entities including central agencies, departments, agencies of the Crown and Memorial University of Newfoundland. This framework should be approved by the House of Assembly, enacted in legislation and specifically require the tabling of annual reports in the House of Assembly.*

## **Comments on Public Sector Accountability**







## CHAPTER

### 3

## Comments on Audits and Additional Examinations

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### 3.1 Monitoring Agencies of the Crown

#### Introduction

As at 31 March 1999 there were approximately 152 (1998 - 156) Crown agencies in the Province. Of these, 83 (1998 - 85) were required to prepare annual financial statements while 69 (1998 - 71) were considered non-financial and did not prepare financial statements. Any expenditures related to the operation of these 69 entities are included with those of the government department responsible for the entity and are audited annually as part of our audit of the public accounts of the Province.

Of the 83 entities required to prepare annual financial statements, 30 (1998 - 29) were audited by our Office while 52 (1998 - 56) were audited by private sector auditors and one has not yet appointed auditors.

Most of these entities do not have any requirement to report to the House of Assembly on the discharge of their responsibilities. As a result, a major role of this Office is to monitor these entities in order to provide some accountability to the House of Assembly. Section 14 of the *Auditor General Act* requires all private sector auditing firms to submit to our Office a copy of the audited financial statements and any management letters for all Crown agencies which they audit. These financial statements and management letters along with our Office's audits of Crown agencies provide the basis for our monitoring of all Crown agencies. The results of our monitoring activities are as follows.

#### Compliance with Section 14

As at 20 January 2000, the information required by Section 14 of the *Auditor General Act* had been received from the private sector auditors for 43 of the 52 entities. Figure 1 provides details of the information received.

Figure 1

**Monitoring Agencies of the Crown**  
**Crown Agencies Audited by Private Sector Auditors**  
**Information for Years Ended**  
**1 April 1998 to 31 March 1999**

| Information                               | Health Care | Education | Other     | Total     |
|-------------------------------------------|-------------|-----------|-----------|-----------|
| Audited financial statements received     | 15          | 14        | 14        | 43        |
| Audited financial statements not received | 4           | 1         | 4         | 9         |
| <b>Total</b>                              | <b>19</b>   | <b>15</b> | <b>18</b> | <b>52</b> |

### 3.1 Monitoring Agencies of the Crown

The 9 agencies noted in Figure 1 for which we have not received audited financial statements are as follows:

- Central West Health Care Institutions Board
- District #10 - Avalon East
- Grenfell Regional Health Services Board
- Health Labrador Corporation
- Multi-Materials Stewardship Board
- Newfoundland Liquor Corporation
- Operation Online
- St. John's Nursing Home Board
- Workplace Health, Safety and Compensation Commission

To date, information is not being received from the private sector auditors on a timely basis. On average, audits are completed and the auditors' reports signed within three months after year end. However, the financial statements are not sent to our Office until another four months after the audit report date, and in most cases, only after telephone follow-up or written correspondence from our Office.

For the years ended between 1 May 1998 and 30 April 1999, our Office was responsible for auditing the financial statements for 30 Crown entities. As at 2 December 1999, the audits of 7 of the 30 entities had not been completed for the year ended 31 March 1999. These included:

#### Department of Development and Rural Renewal

- Enterprise Newfoundland and Labrador Corporation
- Enterprise Network Incorporated
- Farm Development Loan Board
- Fisheries Loan Board of Newfoundland

#### Department of Justice

- Newfoundland Legal Aid Commission
- Office of the High Sheriff

#### Department of Education

- Newfoundland and Labrador Education Investment Corporation

### 3.1 Monitoring Agencies of the Crown

As indicated, four of the seven entities are the responsibility of the Department of Development and Rural Renewal. We note that the Department did not have timely financial statements prepared for us to audit for these four entities in the preceding two years either. In addition to the reduced accountability by not having financial statements prepared, the Department is not providing the financial information necessary for Government to prepare the most accurate and complete financial statements for inclusion in the Public Accounts.

#### Monitoring of Financial Information

In addition to the monitoring of all Crown entities, we also performed an analytical review of the audited financial statements which were available to us. In order to facilitate useful comparisons and analysis of data, a number of sectors were established for grouping similar entities. These sectors and financial information of the various Crown agencies are presented in Figure 2 and Figure 3. These figures do not include financial information for the four Crown agency subsidiaries that have their financial statements consolidated with Newfoundland and Labrador Hydro, their parent company and one recently created Crown agency for which no financial information has yet been received.

Figure 2

**Monitoring of Crown Agencies**  
**Financial Position**  
**Years Ended 1 May 1998 to 30 April 1999**  
**(\$000's)**

| Sector                          | Number of Entities | Current Assets | Long-Term Assets | Current Liabilities | Long-Term Liabilities | Equity      |
|---------------------------------|--------------------|----------------|------------------|---------------------|-----------------------|-------------|
| Primary, Elementary & Secondary | 12                 | \$ 38,523      | \$ 622,036       | \$ 12,258           | \$ 91,033             | \$ 557,268  |
| Colleges & Universities         | 2                  | 56,234         | 163,781          | 162,406             | 16,727                | 40,882      |
| Hospitals & Nursing Homes       | 15                 | 100,972        | 290,957          | 131,842             | 268,536               | (8,449)     |
| Community Health Boards         | 4                  | 9,131          | 2,262            | 10,183              | 7,568                 | (6,358)     |
| Government Enterprises          | 10                 | 201,405        | 2,396,818        | 302,410             | 1,601,211             | 694,602     |
| Financial Entities              | 7                  | 131,258        | 1,373,252        | 58,855              | 382,778               | 1,062,877   |
| Insurance Entities              | 4                  | 22,300         | 300,557          | 6,590               | 408,302               | (92,035)    |
| Judicial Entities               | 4                  | 21,096         | 17,762           | 17,381              | 658                   | 20,819      |
| Pension Plans                   | 2                  | 18,503         | 2,156,769        | 3,257               | -                     | 2,172,015   |
| Other Entities                  | 18                 | 313,782        | 419,639          | 21,499              | 345,161               | 366,761     |
| Total Crown Agencies            | 78                 | \$ 913,204     | \$ 7,743,833     | \$ 726,681          | \$ 3,121,974          | \$4,808,382 |

### 3.1 Monitoring Agencies of the Crown

Figure 3

**Monitoring of Crown Agencies  
Operating Results  
Years Ended 1 May 1998 to 30 April 1999  
(\$000's)**

| Sector                          | Number<br>of<br>Entities | Revenues     | Expenditures | Surplus<br>(Deficit) | Provincial<br>Funding |
|---------------------------------|--------------------------|--------------|--------------|----------------------|-----------------------|
| Primary, Elementary & Secondary | 12                       | \$ 496,047   | \$ 518,887   | \$ (22,840)          | \$ 484,360            |
| Colleges & Universities         | 2                        | 304,467      | 309,109      | (4,642)              | 157,263               |
| Hospitals & Nursing Homes       | 15                       | 849,222      | 841,490      | 7,732                | 769,715               |
| Community Health Boards         | 4                        | 126,287      | 131,367      | (5,080)              | 125,436               |
| Government Enterprises          | 10                       | 510,209      | 352,493      | 157,716              | 3,383                 |
| Financial Entities              | 7                        | 157,056      | 83,798       | 73,258               | 155                   |
| Insurance Entities              | 4                        | 122,516      | 82,424       | 40,092               | 204                   |
| Judicial Entities               | 4                        | 34,291       | 35,051       | (760)                | 5,243                 |
| Pension Plans                   | 2                        | 556,111      | 309,400      | 246,711              | 0                     |
| Other Entities                  | 18                       | 152,124      | 176,047      | (23,923)             | 22,153                |
| Total Crown Agencies            | 78                       | \$ 3,308,330 | \$ 2,840,066 | \$ 468,264           | \$ 1,567,912          |

During our compilation and analysis of the above financial data, the following issues were highlighted:

- Of the 78 (1998 - 77) Crown entities analysed, 19 (1998 - 15) entities reported a total bank indebtedness of \$48.8 million (1998 - \$119.8 million).
- Financial information from the prior year had to be used for a number of entities because the current audited financial statements had not been submitted to our Office or obtainable from other sources. These entities were:
  - Health Labrador Corporation
  - Newfoundland Liquor Corporation
  - St. John's Nursing Home Board
  - Multi-Materials Stewardship Board



### 3.1 Monitoring Agencies of the Crown

- Financial information for 31 March 1998 had to be used for seven entities as the audits for 31 March 1999 had not yet been completed. These entities were:
  - Enterprise Network Incorporated
  - Enterprise Newfoundland and Labrador Corporation
  - Farm Development Loan Board
  - Fisheries Loan Board of Newfoundland
  - Newfoundland and Labrador Education Investment Corporation
  - Newfoundland Legal Aid Commission
  - Office of the High Sheriff

#### Monitoring Management Letters

Section 14 of the *Auditor General Act* requires that management letters prepared by private sector auditors, be submitted to our Office. Of the 52 entities audited by private auditing firms, 14 had no management letters issued, 27 had management letters with weaknesses reported, and 11 entities still had their management letters outstanding as they were not yet finalized. Of the management letters received by our Office from the private sector auditors, many reported control weaknesses such as inadequate segregation of duties, inadequate approval and reconciliation procedures relating to cash, inadequate controls over accounts receivable and accounts payable, inadequate controls over inventory, purchasing and capital assets, human resources issues, pension plan issues, and computer software and hardware deficiencies, including the year 2000 issue. One management letter indicated that a qualified opinion will be issued because of the exclusion from liabilities of vacation and severance entitlements, and tuition and residence fee revenues.

Of the 30 Crown agencies audited by our Office during 1998-99, 6 entities had management letters issued with no control weaknesses reported, 17 had management letters with weaknesses reported, and 7 entities still had their management letters outstanding as they were not yet finalized. Examples of significant weaknesses included non-compliance with governing legislation, inadequate controls over capital assets and investment property, inadequate collection efforts on outstanding accounts receivable, insufficient controls over accounts payable and accounts receivable, poorly maintained records, non-preparation of a budget, and concerns over the year 2000 computer issue.





## 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

### Introduction

As part of our audit of the financial statements of the Consolidated Revenue Fund (CRF), we perform tests and reviews of the expenditures made by the various departments. Figure 1 outlines expenditures, by category, recorded in the Consolidated Revenue Fund financial statements for the years ended 31 March.

Figure 1

### Consolidated Revenue Fund Expenditures By Category Years Ended 31 March (\$ Millions)

| Consolidated Revenue Fund Expenditures |              |              |              |              |              |              |              |              |              |              |
|----------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Category                               | 1990         | 1991         | 1992         | 1993         | 1994         | 1995         | 1996         | 1997         | 1998         | 1999         |
| Salaries and Benefits                  | 396          | 398          | 401          | 407          | 334          | 361          | 347          | 357          | 359          | 286          |
| Transportation and Communication       | 37           | 35           | 34           | 33           | 30           | 33           | 33           | 32           | 32           | 32           |
| Supplies                               | 64           | 62           | 58           | 57           | 49           | 51           | 48           | 48           | 43           | 43           |
| Professional Services                  | 76           | 83           | 85           | 101          | 90           | 64           | 57           | 49           | 52           | 55           |
| Purchased Services                     | 179          | 163          | 152          | 188          | 172          | 183          | 182          | 146          | 169          | 194          |
| Property, Furnishings and Equipment    | 73           | 71           | 79           | 33           | 24           | 43           | 31           | 19           | 23           | 36           |
| Loans and Advances                     | 65           | 62           | 35           | -            | -            | -            | 7            | -            | -            | -            |
| Allowances and Assistance              | 268          | 253          | 282          | 318          | 345          | 372          | 382          | 403          | 385          | 339          |
| Grants and Subsidies                   | 1,492        | 1,705        | 1,770        | 1,801        | 1,744        | 1,770        | 1,780        | 1,754        | 2,123        | 1,839        |
| Debt Expenses                          | 456          | 482          | 488          | 541          | 800          | 904          | 720          | 719          | 766          | 927          |
| Information Technology                 | -            | -            | -            | -            | -            | 27           | 19           | 20           | 27           | 25           |
| Bad Debts                              | -            | -            | -            | 89           | 33           | 33           | 26           | 80           | 28           | 50           |
| <b>Total</b>                           | <b>3,106</b> | <b>3,314</b> | <b>3,384</b> | <b>3,568</b> | <b>3,621</b> | <b>3,841</b> | <b>3,632</b> | <b>3,627</b> | <b>4,007</b> | <b>3,826</b> |

Source: Consolidated Revenue Fund financial statements

## 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

### Introduction

As part of our audit of the financial statements of the Consolidated Revenue Fund (CRF), we perform tests and reviews of the expenditures made by the various departments. Figure 1 outlines expenditures, by category, recorded in the Consolidated Revenue Fund financial statements for the years ended 31 March.

Figure 1

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| Consolidated Revenue Fund Expenditures |              |              |              |              |              |              |              |              |              |              |
|----------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Category                               | 1990         | 1991         | 1992         | 1993         | 1994         | 1995         | 1996         | 1997         | 1998         | 1999         |
| Salaries and Benefits                  | 396          | 398          | 401          | 407          | 334          | 361          | 347          | 357          | 359          | 286          |
| Transportation and Communication       | 37           | 35           | 34           | 33           | 30           | 33           | 33           | 32           | 32           | 32           |
| Supplies                               | 64           | 62           | 58           | 57           | 49           | 51           | 48           | 48           | 43           | 43           |
| Professional Services                  | 76           | 83           | 85           | 101          | 90           | 64           | 57           | 49           | 52           | 55           |
| Purchased Services                     | 179          | 163          | 152          | 188          | 172          | 183          | 182          | 146          | 169          | 194          |
| Property, Furnishings and Equipment    | 73           | 71           | 79           | 33           | 24           | 43           | 31           | 19           | 23           | 36           |
| Loans and Advances                     | 65           | 62           | 35           | -            | -            | -            | 7            | -            | -            | -            |
| Allowances and Assistance              | 268          | 253          | 282          | 318          | 345          | 372          | 382          | 403          | 385          | 339          |
| Grants and Subsidies                   | 1,492        | 1,705        | 1,770        | 1,801        | 1,744        | 1,770        | 1,780        | 1,754        | 2,123        | 1,839        |
| Debt Expenses                          | 456          | 482          | 488          | 541          | 800          | 904          | 720          | 719          | 766          | 927          |
| Information Technology                 | -            | -            | -            | -            | -            | 27           | 19           | 20           | 27           | 25           |
| Bad Debts                              | -            | -            | -            | 89           | 33           | 33           | 26           | 80           | 28           | 50           |
| <b>Total</b>                           | <b>3,106</b> | <b>3,314</b> | <b>3,384</b> | <b>3,568</b> | <b>3,621</b> | <b>3,841</b> | <b>3,632</b> | <b>3,627</b> | <b>4,007</b> | <b>3,826</b> |

Source: Consolidated Revenue Fund financial statements

### **3.2 Monitoring Expenditures of the Consolidated Revenue Fund**

During the past year, we obtained expenditure information from Government's accounting system relating to all expenditures of the Consolidated Revenue Fund. We performed a general review and analysis of amounts paid relating to: grants and subsidies; property, furnishings and equipment; purchased services; professional services; allowances and assistance; and transportation and communications. Details of the expenditures in each of these categories are provided as follows:

#### **Grants and Subsidies**

Government has established programs which provide grants or subsidies to various agencies of the Crown, private corporations and individuals. These payments are made to health care boards, for the operation of the Province's hospitals, to school boards, for the operation of the Province's schools and teachers' salaries, to the College of the North Atlantic and Memorial University of Newfoundland, and to certain agencies of the Crown for operational funding. Other grants and subsidies are paid to private corporations and individuals in accordance with Government support programs.

During the year we continued our process of monitoring and reviewing payments made for grants and subsidies. Figure 2 shows, by department, payments made for grants and subsidies for the year ended 31 March 1999 totalling \$1.839 billion with comparative figures for the year ended 31 March 1998.

As the figure indicates, for the year ended 31 March 1998, payments for grants and subsidies were approximately \$2.12 billion and represented approximately 53% of the total expenditures of the Consolidated Revenue Fund. However, for the year ended 31 March 1999, grants and subsidies amounted to approximately \$1.84 billion or approximately 48.1% of the total expenditures of the Consolidated Revenue Fund.

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 2

**Grants and Subsidies Expenditures  
By Department  
Years Ended 31 March  
(\$000's)**

| Grants and Subsidies Expenditures by Department     |                    |                    |
|-----------------------------------------------------|--------------------|--------------------|
| Department                                          | 1999               | 1998               |
| Health and Community Services                       | \$1,047,572        | \$ 863,352         |
| Education                                           | 680,077            | 670,088            |
| Municipal and Provincial Affairs                    | 45,612             | 120,986            |
| Human Resources and Employment                      | 31,519             | 21,770             |
| Industry, Trade and Technology                      | 10,742             | 11,370             |
| Tourism, Culture and Recreation                     | 10,100             | 14,026             |
| Development and Rural Renewal                       | 9,721              | 10,401             |
| Justice                                             | 5,832              | 5,526              |
| Works, Services and Transportation                  | 5,639              | 22,896             |
| Finance                                             | 5,332              | 352,351            |
| Newfoundland and Labrador Housing Corporation       | 4,733              | 6,324              |
| Fisheries and Aquaculture                           | 4,485              | 6,273              |
| Forest Resources and Agrifoods                      | 3,907              | 14,996             |
| Mines and Energy                                    | 1,138              | 1,441              |
| Environment and Labour                              | 387                | 356                |
| Executive Council                                   | 314                | 298                |
| Legislature                                         | 65                 | 87                 |
| Government Services and Lands                       | 57                 | 49                 |
| Consolidated Fund Services                          | -                  | 506                |
| Reduction in provision for municipal debt repayment | (27,917)           | -                  |
| <b>Total</b>                                        | <b>\$1,839,315</b> | <b>\$2,123,096</b> |

Source: Government's Financial Information System

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

We also summarized the payments of grants and subsidies by the type of entity receiving the payment for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998. The results of this summary are outlined in Figure 3.

**Figure 3**

**Grants and Subsidies Expenditures  
By Type of Entity  
Years Ended 31 March  
(\$000's)**

| Types of Entities Receiving Grants and Subsidies              |           |           |
|---------------------------------------------------------------|-----------|-----------|
| Type of Entity                                                | 1999      | 1998      |
| Hospitals and Health Services Boards                          | \$699,716 | \$622,372 |
| Teachers Payroll                                              | 353,683   | 347,371   |
| Newfoundland Medical Care Commission                          | 174,735   | 161,765   |
| Community Health Boards and Related Entities                  | 155,137   | 66,548    |
| Memorial University of Newfoundland                           | 130,325   | 124,721   |
| School Boards and Related Entities                            | 128,661   | 139,647   |
| Economic Renewal, Labour Market and Industry Support          | 49,064    | 36,093    |
| Municipalities                                                | 45,603    | 120,827   |
| Provincial College                                            | 42,071    | 40,116    |
| Newfoundland and Labrador Education Investment Corporation    | 30,033    | 25,000    |
| Educational Agencies and Post Secondary Education Support     | 6,944     | 6,556     |
| Ferry Operations and Transportation Grants                    | 6,577     | 23,375    |
| Provincial Information and Libraries Resources Board          | 6,364     | 5,860     |
| Labrador Agreement and Native Peoples Support                 | 6,305     | 8,576     |
| Newfoundland Legal Aid Commission                             | 5,696     | 5,263     |
| Newfoundland Municipal Financing Corporation                  | 5,000     | 3,000     |
| Newfoundland and Labrador Housing Corporation                 | 4,733     | 6,324     |
| Marystown Shipyard Subsidy                                    | 3,496     | 3,617     |
| Special Celebrations Corporation of Newfoundland and Labrador | 3,319     | -         |

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 3 (cont'd)

| Types of Entities Receiving Grants and Subsidies       |                    |                    |
|--------------------------------------------------------|--------------------|--------------------|
| Type of Entity                                         | 1999               | 1998               |
| Agricultural Development                               | 2,356              | 2,199              |
| Recreation and Sport                                   | 2,196              | 3,219              |
| Culture and Heritage                                   | 1,510              | 1,459              |
| Canada Newfoundland Offshore Petroleum Board           | 1,016              | 1,334              |
| 1999 Corner Brook Winter Games Host Society            | 593                | -                  |
| Newfoundland and Labrador Film Development Corporation | 550                | -                  |
| Newfoundland Farm Products Corporation                 | 443                | 13,158             |
| C. A. Pippy Park Commission                            | 300                | 872                |
| Labrador Transportation Initiatives Fund               | -                  | 349,172            |
| The John Cabot (500th) Anniversary Celebrations        | -                  | 3,186              |
| Other Miscellaneous Grants                             | 806                | 1,466              |
| Reduction in Provision for Municipal Debt Retirement   | (27,917)           | -                  |
| <b>Total</b>                                           | <b>\$1,839,315</b> | <b>\$2,123,096</b> |

Source: Government's Financial Information System

Figure 4 provides the names of all entities which received funding in excess of \$10 million for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998.



## 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 4

**Grants and Subsidies Expenditures  
Payments in Excess of \$10 million  
Years Ended 31 March  
(\$000's)**

| Entities Which Received in Excess of \$10 Million          |           |           |
|------------------------------------------------------------|-----------|-----------|
| Entity                                                     | 1999      | 1998      |
| Health Care Corporation of St. John's                      | \$290,549 | \$277,881 |
| Newfoundland Medical Care Commission                       | 174,735   | 161,765   |
| Memorial University of Newfoundland                        | 130,325   | 124,721   |
| Western Health Care Corporation                            | 100,153   | 83,649    |
| Central West Health Care Corporation                       | 55,032    | 52,519    |
| Community Health - St. John's                              | 53,373    | 17,754    |
| Central East Health Care Corporation                       | 42,892    | 39,554    |
| College of the North Atlantic                              | 42,071    | 40,116    |
| Peninsulas Health Care Corporation                         | 41,850    | 36,439    |
| Avalon Health Care Corporation                             | 35,323    | 33,558    |
| Eastern Regional Community Health Board                    | 35,018    | 15,771    |
| Central Newfoundland Regional Community Health Board       | 31,238    | 13,971    |
| Newfoundland and Labrador Education Investment Corporation | 30,033    | 25,000    |
| District #10 School Board                                  | 27,762    | 28,740    |
| Grenfell Regional Health Care Corporation                  | 26,625    | 26,512    |
| Labrador Health Services Board                             | 25,881    | 23,478    |
| St. John's Nursing Home Board                              | 21,332    | 209       |
| St. Luke's Home                                            | 20,819    | 4,032     |
| Western Newfoundland Regional Community Health Board       | 13,115    | 11,566    |
| Avalon West School Board                                   | 12,538    | 13,379    |
| Canadian Blood Services                                    | 12,290    | -         |



### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 4 (cont'd)

| Entities Which Received in Excess of \$10 Million                                                      |                    |                    |
|--------------------------------------------------------------------------------------------------------|--------------------|--------------------|
| Entity                                                                                                 | 1999               | 1998               |
| School District #6                                                                                     | 11,123             | 11,207             |
| School District #5                                                                                     | 11,032             | 11,254             |
| Newfoundland Farm Products Corporation                                                                 | 443                | 13,158             |
| Hoyles-Escasoni Complex                                                                                | 4                  | 18,338             |
| Labrador Transportation Initiatives Fund                                                               | -                  | 349,172            |
| Marine Atlantic                                                                                        | -                  | 12,734             |
| Reduction in Provision for Municipal Debt Retirement                                                   | (27,917)           | -                  |
| Grants paid to over 4,300 entities or individuals in 1999 (1998 - over 4,300 entities or individuals). | 621,676            | 676,619            |
| <b>Total</b>                                                                                           | <b>\$1,839,315</b> | <b>\$2,123,096</b> |

Source: Government's Financial Information System

#### Property, Furnishings and Equipment

The Property, Furnishings, and Equipment category generally includes capital items such as equipment purchased for use by Government departments which will have a service life in excess of one year. This category also includes grants made by the Department of Health to the various hospital and health care boards for the purchase of equipment. During the year ended 31 March 1999 the Province paid \$27.4 million (1998 - \$9.4 million) to the hospital and health care boards for equipment which is included in the property, furnishings and equipment category. As indicated in Figure 1, payments for property, furnishings and equipment totalled \$36 million for the year ended 31 March 1999. Figure 5 shows, by department, payments made for property, furnishings and equipment for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998.

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 5

**Property, Furnishings and Equipment Expenditures  
By Department  
Years Ended 31 March  
(\$000's)**

| <b>Property, Furnishings and Equipment Expenditures by Department</b> |                 |                 |
|-----------------------------------------------------------------------|-----------------|-----------------|
| <b>Department</b>                                                     | <b>1999</b>     | <b>1998</b>     |
| Health                                                                | \$27,438        | \$9,441         |
| Works, Services and Transportation                                    | 4,703           | 8,125           |
| Forest Resources and Agrifoods                                        | 1,116           | 1,631           |
| Justice                                                               | 592             | 855             |
| Education                                                             | 570             | 550             |
| Municipal and Provincial Affairs                                      | 464             | 682             |
| Tourism, Culture and Recreation                                       | 373             | 329             |
| Fisheries and Aquaculture                                             | 240             | 315             |
| Government Services and Lands                                         | 238             | 276             |
| Industry, Trade and Technology                                        | 95              | 2               |
| Development and Rural Renewal                                         | 86              | 26              |
| Human Resources and Employment                                        | 85              | 110             |
| Executive Council                                                     | 84              | 77              |
| Mines and Energy                                                      | 71              | 90              |
| Environment and Labour                                                | 38              | 203             |
| Finance                                                               | 36              | 26              |
| Legislature                                                           | 19              | 14              |
| Public Service Commission                                             | 6               | 1               |
| Consolidated Fund Services                                            | 1               | 4               |
| <b>Total</b>                                                          | <b>\$36,255</b> | <b>\$22,757</b> |

Source: Government's Financial Information System

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

We also summarized the payments for property, furnishings and equipment to show all entities which received payments in excess of \$500,000 for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998. These entities are listed in Figure 6.

**Figure 6**

**Property, Furnishings and Equipment Expenditures  
Payments in Excess of \$500,000  
Years Ended 31 March  
(\$000's)**

| <b>Entities Which Received in Excess of \$500,000</b> |                 |                 |
|-------------------------------------------------------|-----------------|-----------------|
| <b>Entity</b>                                         | <b>1999</b>     | <b>1998</b>     |
| Health Care Corporation of St. John's                 | \$8,125         | \$2,445         |
| Newfoundland and Labrador Health Care Association     | 5,000           |                 |
| Western Health Care Corporation                       | 4,775           | 648             |
| Peninsulas Health Care Corporation                    | 2,969           | 720             |
| Labrador Health Services Board                        | 1,363           | 543             |
| Hickman Motors Limited                                | 1,301           | 2,426           |
| The Salvation Army                                    | 1,176           | 1,176           |
| Central West Health Care Corporation                  | 1,023           | 687             |
| Avalon Ford Sales Limited                             | 928             | 1,078           |
| Metalwork Ltd.                                        | 865             | 94              |
| Avalon Health Care Board                              | 828             | 626             |
| Sisters of Mercy Generalate                           | 750             | 750             |
| Grenfel Regional Health Care Board                    | 547             | 293             |
| College of the North Atlantic                         | 500             | 500             |
| Royal Garage Limited                                  | 54              | 728             |
| The Roman Catholic Episcopal Corporation              | -               | 1,061           |
| Harvey and Company Limited                            | -               | 634             |
| O'Reilly, Noseworthy (In Trust)                       | -               | 546             |
| Payments to over 490 entities (1998 - 525 entities)   | 6,051           | 7,802           |
| <b>Total</b>                                          | <b>\$36,255</b> | <b>\$22,757</b> |

Source: Government's Financial Information System

## 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

### Purchased Services

Purchased services includes such services as heat and light, general maintenance, printing, vehicle rentals and repairs, advertising, and insurance. As indicated in Figure 1, payments for purchased services totalled \$194 million for the year ended 31 March 1999. Figure 7 shows, by department, payments made for purchased services for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998.

Figure 7

#### Purchased Services Expenditures By Department Years Ended 31 March (\$000's)

| Purchased Services Expenditures by Department |                  |                   |
|-----------------------------------------------|------------------|-------------------|
| Department                                    | 1999             | 1998              |
| Works, Services and Transportation            | \$151,497        | \$ 122,158        |
| Forest Resources and Agrifoods                | 8,933            | 11,906            |
| Education                                     | 5,775            | 7,037             |
| Tourism, Culture and Recreation               | 5,361            | 6,759             |
| Justice                                       | 5,123            | 5,031             |
| Municipal and Provincial Affairs              | 3,077            | 3,047             |
| Industry, Trade and Technology                | 3,060            | 1,781             |
| Development and Rural Renewal                 | 2,232            | 1,543             |
| Government Services and Lands                 | 1,985            | 1,841             |
| Human Resources and Employment                | 1,624            | 3,087             |
| Fisheries and Aquaculture                     | 1,325            | 1,443             |
| Executive Council                             | 1,139            | 925               |
| Legislature                                   | 829              | 769               |
| Health and Community Services                 | 615              | 141               |
| Environment and Labour                        | 552              | 597               |
| Mines and Energy                              | 456              | 371               |
| Consolidated Fund Services                    | 389              | 201               |
| Finance                                       | 254              | 213               |
| Public Service Commission                     | 203              | 227               |
| <b>Total</b>                                  | <b>\$194,429</b> | <b>\$ 169,077</b> |

Source: Government's Financial Information System

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

We also summarized the payments for purchased services to show all entities which received payments in excess of \$1 million for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998. These entities are listed in Figure 8.

**Figure 8**

**Purchased Services Expenditures  
Payments in Excess of \$1 million  
Years Ended 31 March  
(\$000's)**

| Entities Which Received in Excess of \$1 Million |          |          |
|--------------------------------------------------|----------|----------|
| Entity                                           | 1999     | 1998     |
| S M Construction                                 | \$16,962 | \$11,353 |
| Western Construction Co. Ltd                     | 7,285    | 12,366   |
| Labrador Construction Limited                    | 5,958    | 2,102    |
| Municipal Construction Ltd.                      | 5,911    | 1,624    |
| Newfoundland Power                               | 5,714    | 6,136    |
| Pennecon Ltd                                     | 4,606    | 4,236    |
| Provincial Paving                                | 4,257    | 5,910    |
| Colby Construction Ltd.                          | 4,205    | 1,562    |
| Penney Paving                                    | 4,102    | 6,593    |
| MCNamara Construction Company                    | 4,099    | 8,427    |
| J-1 Contracting Limited                          | 3,839    | 4,477    |
| 10663 Newfoundland Limited                       | 3,817    | -        |
| Pyramid Construction                             | 3,567    | 419      |
| Trident Construction Limited                     | 3,023    | 2,476    |
| Weirs Construction Co Ltd                        | 2,941    | 1,062    |
| College of the North Atlantic                    | 2,742    | 2,149    |
| St. John's Dockyard Limited                      | 2,309    | 834      |
| Coady's Construction and Excavating Ltd.         | 2,283    | 22       |
| Bristol Communications Ltd.                      | 2,199    | 805      |
| Central East Health Care Board                   | 2,096    | 65       |

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 8 (cont'd)

| Entities Which Received in Excess of \$1 Million                                       |                  |                  |
|----------------------------------------------------------------------------------------|------------------|------------------|
| Entity                                                                                 | 1999             | 1998             |
| Target Marketing Inc.                                                                  | 1,999            | 2,327            |
| Brook Enterprises Inc.                                                                 | 1,982            | 872              |
| Johnson Construction Ltd.                                                              | 1,936            | 399              |
| Canship Limited                                                                        | 1,810            | -                |
| Mariner Engineering                                                                    | 1,679            | 94               |
| Northern Cruiser Ltd.                                                                  | 1,623            | 7                |
| RDN Construction                                                                       | 1,604            | 1,880            |
| Humber Valley Paving                                                                   | 1,599            | 977              |
| Marine Contractors Inc.                                                                | 1,594            | -                |
| J&H Marsh & McLennan Limited                                                           | 1,581            | 1,549            |
| Glenn Corp Ltd.                                                                        | 1,438            | 1,252            |
| Newfoundland and Labrador Forestry Training Association                                | 1,437            | -                |
| Land and Sea Welding Limited                                                           | 1,318            | 72               |
| Barkers Construction Limited                                                           | 1,308            | 1,079            |
| Puddister Trading Company Ltd.                                                         | 1,210            | -                |
| Nova Services Ltd.                                                                     | 1,167            | 1,157            |
| Budgells Equipment and Rental                                                          | 1,036            | 654              |
| Memorial University of Newfoundland                                                    | 588              | 3,790            |
| Merit Management Inc.                                                                  | 494              | 2,896            |
| Receiver General for Canada                                                            | 466              | 1,266            |
| Concord Paving Limited                                                                 | 353              | 2,138            |
| Council of Higher Education                                                            | 285              | 1,581            |
| Northland Contracting Inc.                                                             | 139              | 3,916            |
| Payments to over 5,600 entities or individuals (1998 - 5,900 entities or individuals). | 73,868           | 68,553           |
| <b>Total</b>                                                                           | <b>\$194,429</b> | <b>\$169,077</b> |

Source: Government's Financial Information System



### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

#### Professional Services

Professional services generally include the fees and expenses of those engaged in a specialty profession such as accountants, doctors, lawyers, and engineers who provide a service, a report or advice to Government. As indicated in Figure 1, payments for professional services totalled \$55 million for the year ended 31 March 1999. Figure 9 shows, by department, payments made for professional services for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998.

Figure 9

**Professional Services Expenditures  
By Department  
Years Ended 31 March  
(\$000's)**

| Professional Services Expenditures by Department |                 |                 |
|--------------------------------------------------|-----------------|-----------------|
| Department                                       | 1999            | 1998            |
| Justice                                          | \$36,401        | \$ 36,369       |
| Consolidated Fund Services                       | 5,469           | 5,462           |
| Works, Services and Transportation               | 3,994           | 3,306           |
| Health and Community Services                    | 1,611           | 1,508           |
| Environment and Labour                           | 1,337           | 1,044           |
| Executive Council                                | 943             | 453             |
| Municipal and Provincial Affairs                 | 840             | 572             |
| Development and Rural Renewal                    | 642             | 972             |
| Forest Resources and Agriculture                 | 554             | 304             |
| Government Services and Lands                    | 498             | 410             |
| Mines and Energy                                 | 437             | 256             |
| Industry, Trade and Technology                   | 399             | 175             |
| Human Resources and Employment                   | 395             | 406             |
| Tourism, Culture and Recreation                  | 252             | 302             |
| Education                                        | 216             | 292             |
| Finance                                          | 195             | 373             |
| Fisheries and Aquaculture                        | 129             | 161             |
| Public Service Commission                        | 112             | 87              |
| Legislature                                      | 65              | 21              |
| <b>Total</b>                                     | <b>\$54,489</b> | <b>\$52,473</b> |

Source: Government's Financial Management Information System

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

We also summarized the payments of professional services to show all entities which received payments in excess of \$100,000 for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998. These entities are listed in Figure 10.

**Figure 10**

**Professional Services Expenditures  
Entities paid in Excess of \$100,000  
Years Ended 31 March  
(\$000)'s**

| Entities Which Received in Excess of \$100,000                |          |          |
|---------------------------------------------------------------|----------|----------|
| Entity                                                        | 1999     | 1998     |
| Receiver General For Canada (RCMP Contract etc.)              | \$35,126 | \$34,898 |
| Newtel Information Solutions                                  | 922      | 883      |
| Bae-Newplan Group Ltd                                         | 878      | 1,314    |
| Newfoundland Design Associates Ltd.                           | 684      | 163      |
| Jacques Whitford Environment                                  | 574      | 6        |
| Newfoundland Government Fund                                  | 395      | -        |
| The SGE Group Inc.                                            | 324      | 215      |
| Patterson Palmer Hunt Murphy                                  | 316      | 736      |
| Stratcona Mineral Service Ltd.                                | 269      | -        |
| Agra Monenco Atlantic Inc. (formerly BFL Consultants Limited) | 247      | 144      |
| Goss Gilroy Inc.                                              | 223      | 12       |
| Central East Health Care Board                                | 189      | -        |
| Health Care Corporation of St. John's                         | 181      | 280      |
| Benson Myles                                                  | 164      | 167      |
| Blue Cross of Atlantic Canada                                 | 127      | 25       |
| Chalker, Green and Rowe                                       | 126      | 42       |
| A D Tupper and Associated Ltd.                                | 122      | 15       |
| William Mac Cullium Architect                                 | 114      | 19       |
| Misoco                                                        | 110      | -        |
| Walbourne Design Associates                                   | 110      | 10       |



## 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 10 (cont'd)

| Entities Which Received in Excess of \$100,000                                    |                 |                 |
|-----------------------------------------------------------------------------------|-----------------|-----------------|
| Entity                                                                            | 1999            | 1998            |
| Terpstra and Associates                                                           | 106             | 59              |
| Memorial University of Newfoundland                                               | 76              | 183             |
| Nova Consultants Inc.                                                             | 32              | 142             |
| A E Consultants Ltd                                                               | 28              | 434             |
| Harris & Associates Ltd.                                                          | 26              | 114             |
| Martin Whelan Hennebury and Stamp                                                 | 22              | 114             |
| Andy Rowe Consultants                                                             | 18              | 158             |
| French, Browne                                                                    | 1               | 146             |
| Rose Technology Group Ltd.                                                        | -               | 145             |
| Payments to over 750 entities or individuals (1998 - 790 entities or individuals) | 12,979          | 12,049          |
| <b>Total</b>                                                                      | <b>\$54,489</b> | <b>\$52,473</b> |

Source: Government's Financial Information System

### Allowances and Assistance

Allowances and assistance expenditures include costs relating to such items as: allowances for Members of the House of Assembly, social assistance allowances paid to individuals, out of court settlements, and allowances paid on behalf of individuals to organizations. As indicated in Figure 1, payments for allowances and assistance totalled \$339 million for the year ended 31 March 1999. Figure 11 shows, by department, payments made for allowances and assistance for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998.

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

Figure 11

**Allowances and Assistance Expenditures  
By Department  
Years Ended 31 March  
(\$000's)**

| Allowances and Assistance Expenditures by Department |                  |                  |
|------------------------------------------------------|------------------|------------------|
| Department                                           | 1999             | 1998             |
| Human Resources and Employment                       | \$235,334        | \$309,256        |
| Health and Community Services                        | 71,680           | 55,844           |
| Education                                            | 19,654           | 15,157           |
| Justice                                              | 7,782            | 427              |
| Legislature                                          | 4,354            | 4,050            |
| Works, Services and Transportation                   | 190              | 210              |
| Municipal and Provincial Affairs                     | 182              | 224              |
| Environment and Labour                               | 118              | 116              |
| Public Service Commission                            | 84               | -                |
| Executive Council                                    | 32               | 32               |
| Forest Resources and Agrifoods                       | 20               | 15               |
| Tourism, Culture and Recreation                      | 2                | 30               |
| <b>Total</b>                                         | <b>\$339,432</b> | <b>\$385,361</b> |

Source: Government's Financial Management Information System

We also summarized the payments of allowances and assistance to show all entities which received payments in excess of \$500,000 with comparative figures for the year ended 31 March 1998. These entities are listed in Figure 12.

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

**Figure 12**

**Allowances and Assistance Expenditures  
Entities paid in Excess of \$500,000  
Years Ended 31 March  
(\$000's)**

| <b>Individuals or Entities Which Received in Excess of \$500,000</b>                                                    |                  |                  |
|-------------------------------------------------------------------------------------------------------------------------|------------------|------------------|
| <b>Entity</b>                                                                                                           | <b>1999</b>      | <b>1998</b>      |
| Cox, Hanson O'Reilly                                                                                                    | \$4,200          | \$ -             |
| Newfoundland and Labrador Housing Corporation                                                                           | 2,088            | 2,177            |
| Heywood, Kennedy, Belbin                                                                                                | 1,750            | -                |
| Health Care Corporation of St. John's                                                                                   | 1,252            | 1,527            |
| Moores, Andrews                                                                                                         | 1,221            | -                |
| Memorial University of Newfoundland                                                                                     | 768              | 4,538            |
| Fewers Ambulance Service                                                                                                | 541              | 467              |
| Eastern Residential Tenancies Board                                                                                     | 1                | 1,463            |
| St. Francis Foundation                                                                                                  | -                | 1,296            |
| Choices For Youth                                                                                                       | -                | 795              |
| Daybreak Parent Child Centre                                                                                            | -                | 732              |
| Vital Aire                                                                                                              | -                | 725              |
| Memorial United Church Group                                                                                            | -                | 696              |
| Gambo Group Home                                                                                                        | -                | 656              |
| Pine Heights Residence Association                                                                                      | -                | 581              |
| Bay St George Youth Assessment                                                                                          | -                | 558              |
| Labrador Group Home                                                                                                     | -                | 516              |
| Gander Regional Youth                                                                                                   | -                | 515              |
| Miscellaneous amounts under \$500,000 paid to over 1,650 entities or individuals (1998 - 2,000 entities or individuals) | 327,611          | 368,119          |
| <b>Total</b>                                                                                                            | <b>\$339,432</b> | <b>\$385,361</b> |

Source: Government's Financial Information System

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

#### Transportation and Communications

Transportation and communications expenditures include costs relating to such items as: postage, freight, ambulance and air services, telecommunication services and travel for ministers, government employees and others. As indicated in Figure 1, payments for transportation and communications totalled \$32 million for the year ended 31 March 1999. Figure 13 shows, by department, payments made for transportation and communications for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998.

Figure 13

#### Transportation and Communications Expenditures By Department Years Ended 31 March (\$000's)

| Transportation and Communications Expenditures by Department |                 |                 |
|--------------------------------------------------------------|-----------------|-----------------|
| Department                                                   | 1999            | 1998            |
| Works, Services and Transportation                           | \$6,156         | \$5,293         |
| Forest Resources and Agrifoods                               | 4,885           | 4,459           |
| Justice                                                      | 3,155           | 3,277           |
| Government Services and Lands                                | 1,978           | 1,939           |
| Human Resources and Employment                               | 1,975           | 3,883           |
| Education                                                    | 1,887           | 1,691           |
| Tourism, Culture and Recreation                              | 1,640           | 1,719           |
| Executive Council                                            | 1,525           | 1,282           |
| Health and Community Services                                | 1,169           | 466             |
| Mines and Energy                                             | 1,165           | 1,057           |
| Fisheries and Aquaculture                                    | 1,037           | 972             |
| Development and Rural Renewal                                | 937             | 1,143           |
| Environment and Labour                                       | 872             | 895             |
| Industry, Trade and Technology                               | 852             | 757             |
| Finance                                                      | 833             | 936             |
| Legislature                                                  | 711             | 714             |
| Municipal and Provincial Affairs                             | 670             | 1,019           |
| Consolidated Fund Services                                   | 158             | 129             |
| Public Service Commission                                    | 115             | 64              |
| <b>Total</b>                                                 | <b>\$31,720</b> | <b>\$31,695</b> |

Source: Government's Financial Management Information System

### 3.2 Monitoring Expenditures of the Consolidated Revenue Fund

We also summarized the payments for transportation and communications to show all entities which received payments in excess of \$100,000 for the year ended 31 March 1999 with comparative figures for the year ended 31 March 1998. These entities are listed in Figure 14.

Figure 14

**Transportation and Communications  
Expenditures  
Entities Paid in Excess of \$100,000  
Years Ended 31 March  
(\$000's)**

| <b>Entities Which Received in Excess of \$100,000</b>                                                                   |                 |                 |
|-------------------------------------------------------------------------------------------------------------------------|-----------------|-----------------|
| <b>Entity</b>                                                                                                           | <b>1999</b>     | <b>1998</b>     |
| Newfoundland Telephone Company (Contract)                                                                               | \$4,388         | \$5,186         |
| Postage by Phone                                                                                                        | 2,143           | 2,350           |
| Universal Helicopters Nfld. Ltd                                                                                         | 2,034           | 1,772           |
| Newtel Communications Inc. .                                                                                            | 1,630           | 1,691           |
| Newtel Mobility Limited                                                                                                 | 1,197           | 870             |
| Harvey's Travel                                                                                                         | 794             | 465             |
| Canada Post Corporation                                                                                                 | 713             | 666             |
| Canadian Helicopters Limited                                                                                            | 653             | 598             |
| Provincial Airlines Limited                                                                                             | 457             | 532             |
| Legrow's Travel                                                                                                         | 401             | 413             |
| Newfoundland and Labrador Air Transport Ltd.                                                                            | 354             | 333             |
| Newfoundland Helicopters Ltd.                                                                                           | 326             | 186             |
| Newfoundland and Labrador Hydro                                                                                         | 195             | 165             |
| City of St. John's                                                                                                      | 167             | 167             |
| Telemedicine Centre                                                                                                     | 146             | 1               |
| Supermarine Aircraft                                                                                                    | 130             | -               |
| Labrador Airways Limited                                                                                                | 22              | 102             |
| V Kelner Airways Limited                                                                                                | 10              | 128             |
| Miscellaneous amounts under \$100,000 paid to over 8,700 individuals or entities (1998 - 7,500 individuals or entities) | 15,960          | 16,070          |
| <b>Total</b>                                                                                                            | <b>\$31,720</b> | <b>\$31,695</b> |

Source: Government's Financial Information System

### 3.3 The Canada-Newfoundland Economic Renewal Agreement

#### Introduction

The Canada-Newfoundland Economic Renewal Agreement (ERA) was signed on 20 June 1996. The Agreement is between the Federal and Provincial Governments and covers the period 1 April 1996 through 31 March 2001. Its purpose "is to increase opportunities for economic development in Newfoundland and, specifically, to enhance growth of earned incomes and employment opportunities in the province." The primary focus of the Agreement is on advanced technology, tourism and aquaculture. Funding under the ERA totals \$100 million, cost-shared between the Federal Government (\$80 million) and the Provincial Government (\$20 million). Figure 1 provides information on the funding allocated to each program area and the actual program expenditures to 31 March 1999.

Figure 1

#### ERA Program Funding and Expenditures \$Million

| Program                  | Original<br>Funding<br>Allocation | Revised Funding<br>Allocation | Expenditures<br>31 March 1999 |
|--------------------------|-----------------------------------|-------------------------------|-------------------------------|
| Advanced Technology      | \$36.29                           | \$37.99                       | \$13.62                       |
| Tourism                  | 22.85                             | 26.85                         | 20.95                         |
| Aquaculture              | 20.00                             | 20.00                         | 16.28                         |
| Forest Ecosystems Centre | 5.00                              | 5.69                          | 5.69                          |
| Strategic Planning       | 2.00                              | 1.70                          | .72                           |
| Youth Ventures           | .75                               | .75                           | .35                           |
| Other Initiatives        | 6.10                              | .01                           | -                             |
| Administration           | 7.01                              | 7.01                          | 4.16                          |
| <b>Total</b>             | <b>\$100.00</b>                   | <b>\$100.00</b>               | <b>\$61.77</b>                |

Source: Original and revised Schedule "B" of the ERA and the 31 March 1999 ERA Financial Summary Worksheet



### **3.3 The Canada-Newfoundland Economic Renewal Agreement**

The administration and management of the Agreement is the responsibility of a Management Committee which consists of a Federal and Provincial co-chair who are jointly appointed by the Federal and Provincial Governments. For each program area, the Management Committee has established Implementation Committees to which it has delegated many of its responsibilities under the Agreement. The Implementation Committees consist of a Federal and Provincial co-chair appointed by the Management Committee and other senior Federal and Provincial officials involved in the administration of the particular program. All projects under each program are administered by either the Federal or Provincial Government.

#### **Scope and Objectives**

We reviewed the overall management and administration of the Agreement. We completed our review in February 1999. Our objectives were to:

- determine whether programs and the various projects under each program are adequately monitored to assess their progress; and
- determine whether programs and the various projects under each program are adequately evaluated to ensure that the objectives of the Agreement are being achieved.

In addition, we reviewed nine projects which received \$7.8 million of ERA funding under the Tourism Program to determine whether the Management Committee was complying with the provisions of the Agreement.

We also reported on the Aquaculture Program component of the Economic Renewal Agreement in our 1998 Report to the House of Assembly.

#### **Conclusions**

The Canada-Newfoundland Economic Renewal Agreement was signed on 20 June 1996 to increase opportunities for economic development in Newfoundland and specifically to enhance growth of earned incomes and employment opportunities in the Province. The Agreement covers the period 1 April 1996 to 31 March 2001 and provides funding of \$100 million, cost shared between the Federal Government (\$80 million) and the Provincial Government (\$20 million). The Agreement is comprehensive and specifically defines what is required to implement, monitor and manage the Agreement.

### 3.3 The Canada-Newfoundland Economic Renewal Agreement

Our review indicated that from 1996 to 1998 there has been a steady improvement of the implementation, monitoring and management of the Agreement programs and projects. Further improvements are required and we were informed that further improvements are planned.

Our review identified two significant weaknesses which should be addressed:

- Under the Agreement, the Management Committee has the right to examine and audit the records of projects managed by third party individuals and organizations who have received funding under the Agreement. As of March 1999, these third party individuals and organizations have received \$51 million in project funding. However, no inspection or audit of these records and supporting invoices has been carried out to date. As a result, Government cannot demonstrate that all expenditures made by third parties under the Agreement were eligible for ERA funding.
- Although the Management Committee established an Evaluation Framework as required under the Agreement and some useful information is being provided through this Framework, adequate performance information necessary to evaluate the programs is not being provided by all of the implementing departments. In addition, since key performance targets were not included in the third party contracts there is no formal requirement for these third parties to provide this information. As a result, it will not be possible for the Management Committee to evaluate whether the objectives of the Agreement are being achieved.

Our review of the nine projects selected under the Tourism Program indicated that the Management Committee has complied, for the most part, with terms of the Agreement. The review, however, identified the following main weaknesses: all calls for tenders and announcements on the award of contracts were not approved by the Management Committee and the Management Committee did not ensure that third parties complied with all relevant Federal and Provincial legislation.

#### **Findings and Recommendation**

#### **Monitoring Programs**

Effective monitoring of the progress of programs and the individual projects is essential to determine whether program objectives are being achieved, funds are being spent for their intended purpose, and problems are detected early during implementation of the Agreement, thus providing a basis for refinement. The Agreement requires that the programs and the individual projects be properly managed through the preparation of annual work plans, financial and management information



### **3.3 The Canada-Newfoundland Economic Renewal Agreement**

reports, the conduct of regular meetings, a review of the Agreement strategy, programming and budget, and the inspection and audit of projects. Our review of this area indicated the following:

#### **1. Annual Work Plans**

The Agreement requires that, before the commencement of each fiscal year, the Management Committee approve an annual work plan identifying projects to be implemented during the fiscal year, the implementing parties, the estimated completion dates and the budgeted eligible costs. Responsibility for preparation of annual work plans has been delegated by the Management Committee to the Implementation Committees.

During 1996/97, the first year of the Agreement, detailed work plans were not prepared for any of the programs. In that year, \$15 million of the \$25 million budgeted was spent. In 1997/98, detailed work plans were prepared for all programs; however, these plans were not approved by the Management Committee until one month after the fiscal year had commenced. Annual Work Plans for 1998/99 were prepared and approved by the Management Committee prior to commencement of that fiscal year. Thus, although there were problems in preparing Annual Work Plans during the initial stages of implementing the Agreement, the Implementation Committees are now ensuring compliance with the Agreement.

#### **2. Financial and Management Information Reports**

The Agreement requires the Management Committee to prepare, on a quarterly and annual basis, financial and management information reports on the project and program expenditures of previous fiscal years, up-to-date cash flows during the current fiscal year and anticipated cash flows during the remaining fiscal year. In reviewing the reporting policies adopted by the Management Committee, it was noted that responsibility for preparation of reports has been delegated to the Implementation Committees. During the first year of the Agreement, the Management Committee increased the frequency of reporting from quarterly to monthly. Effective August 1997, quarterly reporting requirements were adopted. In reviewing the reports it was noted that:

- During the first year of the Agreement, the Implementation Committees were not consistently preparing monthly management information reports. Since the Management Committee no longer required monthly management information reports as of August 1997, quarterly management information reports as required by the Agreement have been submitted on a timely basis with a few exceptions.

### 3.3 The Canada-Newfoundland Economic Renewal Agreement

- During the first two and a half years of the Agreement, the financial information presented to the Management Committee by the Implementation Committees was incomplete and inconsistent. For example, some management information reports did not contain cash flow information or expenditures to date and each program was submitting information in different formats, making it difficult for the Management Committee to make comparisons between the progress of various programs. In addition, although the Management Committee received financial information on each individual program and the various related projects, there was no overall financial report for the entire Agreement to facilitate decisions such as the re-profiling (i.e. reallocating) of funds from one program to another.

To address these concerns, effective 30 September 1998, a new financial report was adopted by each Implementation Committee to track cash flow information with an overall summary for expenditures to date. A review of this new financial report indicated that improvement has been made both in the completeness and consistency of information. However, to comply with the Agreement and further improve financial management, this report should project expenditures to the end of the Agreement.

#### 3. Meetings

The Agreement requires the Management Committee to meet at least quarterly. This requirement has also been applied to the Implementation Committees. Quarterly meetings are required in order to administer and manage the Agreement and coordinate all aspects of the Agreement with other Federal and Provincial programs. The Agreement also outlines a number of responsibilities of the Management Committee vis a vis the quarterly meetings. Our review indicated the following:

- Not all Implementation Committees have met quarterly since the effective date of the Agreement. For example, Aquaculture did not meet in the first quarter of 1997/98 and the first and third quarter of 1998/99, Advanced Technology did not meet in the third quarter of 1996/97 and Tourism did not meet in the fourth quarter of 1996/97 and the first and fourth quarter of 1997/98.
- Minutes for all Implementation Committee meetings are to be forwarded, under accepted practice, to the Executive Coordinator. In the case of minutes for the Committee responsible for implementing the Tourism Program, no minutes had been forwarded to the Executive Coordinator from January 1998 to the end of our review in February 1999.

### **3.3 The Canada-Newfoundland Economic Renewal Agreement**

#### **4. Review of Agreement Strategy, Programming and Budget**

The Agreement requires the Management Committee, on an annual basis, to review the strategy, programming and budget as set out in Schedule A of the Agreement. This review is documented in the 1997 and 1998 ERA annual reports which were prepared by the Management Committee.

These reports provided, in varying levels of detail for each program, a description of projects, the activity to date, a work plan for the upcoming year and actual and budget information. Although the reports did review the status of programs being delivered, they do not present a detailed annual budget for the remaining years of the Agreement. Thus, the reports do not reflect the impact that the re-profiling of funding from one year to another and among programs has on the objectives of the Agreement. For example, in 1996/97, the total budget was \$25 million with total actual expenditures of \$15 million and in 1997/98, the total budget was \$32 million with total actual expenditures of \$27 million.

#### **5. Inspection and Audit Procedures**

Provincially administered projects are either managed directly by the Department responsible or by a third party contracted by the Department. For those projects managed directly by the Department, all supporting invoices would be on file. For those projects managed by third parties, supporting invoices are generally not on file at the Department. However, the Agreement allows the Department to inspect and audit the records of these third parties. Exercising these rights on a timely basis enhances the reliability of the financial information and therefore facilitates effective management of the Agreement.

Our review indicated that an external audit of the Agreement expenditures for the two years ended 31 March 1997 and 1998 was completed in January of 1999. However, this audit did not include a review of the records of these third parties. In July 1998, the Management Committee hired a Compliance Officer to conduct audits on third parties. However, as of February 1999, no audits have been conducted. As a result, Government cannot demonstrate that all expenditures made by third parties under the Agreement, which total \$51 million at the end of March 1999, were eligible for ERA funding. In addition, there are no policies to address issues such as who is responsible for requesting or initiating the audit, when the audit should occur and mechanisms to recover ineligible expenditures.

### 3.3 The Canada-Newfoundland Economic Renewal Agreement

#### Program Evaluation

To ensure that objectives of the Agreement and the various individual projects have been achieved, the Agreement requires the development of an Evaluation Framework within six months of signing the Agreement and a comprehensive evaluation report within six months before the termination of the Agreement. However, the final monitoring and evaluation framework was not approved by the Management Committee until 16 February 1998, over a year after the required date. The Evaluation Framework is to address such issues as who is responsible for the evaluation and data collection, the type and timing of data collection, and the provision of baseline studies, monitoring of industry trends and program status reports.

Our review indicated that significant efforts and resources have been provided to the development of an evaluation framework and the definition of performance indicators. Our review of the Evaluation Framework and subsequent discussions with officials have indicated that although this framework is providing the Management Committee with some useful information, a number of issues have been identified which will have to be resolved in order to effectively evaluate the program.

- For each of the projects funded under the Agreement, Schedule B specifies various economic benefits and job creation potential. To measure the achievement of these economic benefits and job creation potential, targets or key results are required to be included in the Evaluation Framework. Our review indicated that many of these targets were not included in the Evaluation Framework. Without this information, it will not be possible to determine whether the economic benefits and job creation have been achieved.
- In many cases where targets or key results were included in the Evaluation Framework, baseline information and performance data was not available to determine whether the economic benefits and job creation has been achieved.

### 3.3 The Canada-Newfoundland Economic Renewal Agreement

- Roles and responsibilities for data collection, including how often data should be collected and who should be collecting it, have not been adequately defined or communicated to the appropriate officials. For example, discussion with a Departmental official indicated that the responsibility for co-ordinating the collection of data for the Tourism program has not been formally assigned to anyone. Furthermore, another Departmental official specified in the Evaluation Framework as responsible for the provision of data on several other projects was no longer working with the Department and no one had been reassigned this responsibility.
- Although performance data for certain projects is to be provided by a third party, this requirement is not included in the third party contracts for the projects that we reviewed. The data that is provided by third parties is not verified.
- The Framework provides for an annual monitoring report on progress for program activities, annual industry profiles and economic well-being measures for impact areas. The first monitoring report on the Agreement was presented in the 1997/98 Annual Report. A review of this report indicated that not all of the implementing departments are gathering and providing the necessary data to monitor the progress of their respective programs in relation to the objectives of the Agreement.

#### Compliance with Agreement

We reviewed nine projects which received \$7.8 million of ERA funding under the Tourism program to determine whether the Management Committee was complying with the provisions of the Agreement. Our review indicated that the Management Committee has complied, for the most part, with the Agreement. However, the following weaknesses were noted:

- A disbursement in the amount of \$150,000 relating to one project was made before the project was formally approved by the Management Committee.
- For the most part, the third party contracts did not define what types of expenditures could be considered "eligible costs" and funded under the ERA program. In addition, there was no direction regarding the disposition of assets funded under the Agreement.



### 3.3 The Canada-Newfoundland Economic Renewal Agreement

- The Agreement requires that the Management Committee approve all calls for tenders and announcements on the awarding of contracts. This responsibility was delegated by the Management Committee to the Implementation Committees. Our review of projects funded through organizations or individuals indicated that the Committees are not approving all calls for tenders and announcement of contract awards.
- The Agreement requires that all relevant and applicable Federal and Provincial legislation and policies apply to all projects. Examples of Provincial legislation and policies include the *Public Tender Act* and Government's policy on the awarding of consulting contracts. Compliance with this requirement has not been included in any contracts with organizations and individuals receiving funding under the Agreement. In addition, there are no policies to ensure compliance with this requirement.

In March 1999, a round table discussion was held on this issue with the objective of formulating a policy which would address the requirements of the Agreement.

- In order to provide consistent recognition for Agreement activities and promote accessibility to its funding, the Agreement requires the Management Committee to develop, manage and evaluate an annual communications plan. To address this requirement, a Communications Officer was hired to plan and coordinate communication activities for the Agreement. Our review indicated that a formal annual communications plan is not being prepared; however, a five year communication plan was developed at the onset of the Agreement. In addition, the Communications Officer is actively involved with the Implementation Committees in planning and coordinating ongoing communications activities. The Communication Officer also reports regularly to the Management Committee on these plans and activities.

In May of 1997, at the request of the Executive Co-ordinator of the Agreement, the Internal Audit Division of the Treasury Board Secretariat completed a review of the initial year of the Agreement. This review was conducted to determine whether procedures were carried out in accordance with the terms of the Agreement. The internal audit report identified several weaknesses regarding the administration and management of the Agreement which, with the exception of the lack of an annual communications plan, have been adequately addressed by the Management Committee.

### **3.3 The Canada-Newfoundland Economic Renewal Agreement**

#### **Recommendation**

*The findings in the report should be reviewed and appropriate action taken as deemed necessary.*

#### **Executive Council's Response**

*We have reviewed your observations and recommendation as outlined in the report and would like to inform you that appropriate action will be taken to address the concerns indicated. For your information, compliance audits have been started on several third party projects funded through the agreement and this will now be an ongoing process.*

*Under this federal/provincial agreement there has been a real conscious effort made to effectively deliver, manage and monitor the agreement.*

### 3.4 Special Warrants

#### Introduction

The common parliamentary means of providing spending authority to government for its operations is through the annual passing of supply acts. This involves having the Members of the House of Assembly vote on the government's funding requests before the spending authority is provided. Approval by a majority of the Members of the House of Assembly is needed to pass an act.

Through the use of a "special warrant", Government can, without the prior approval of the Members of the House of Assembly, spend public money. Section 28 of the *Financial Administration Act* outlines two instances where a special warrant can be approved and additional funding can be provided to government.

- Section 28(2) states where the sum appropriated by the Legislature for a continuing service is insufficient to meet requirements and there are no countervailing savings available, and **the necessity is urgent**, then the Lieutenant-Governor in Council may order that a special warrant be prepared for the Lieutenant-Governor's signature.
- Section 28(3) states where the Legislature is not in session or when the House of Assembly has been adjourned for more than 30 days, and an expenditure not foreseen and not provided for by the Legislature for a new service is urgently and immediately required for the public good, then the Lieutenant-Governor in Council may order that a special warrant be prepared for the Lieutenant-Governor's signature. The minister having charge of the new service must be of the opinion that **the necessity is urgent** and if not made, grave damage to the interests of the Crown or the public will result.

The *Financial Administration Act* also requires that each Minute of Council authorizing a special warrant quote the special reasons for doing so, and a certified copy of the Minute of Council and the special warrant has to be tabled in the House of Assembly. In the case of a special warrant issued under subsection (2) while the Legislature is in session, tabling is required within 3 days of the issue of the special warrant. In all other cases, tabling is required within 15 days from the opening of the next ensuing session of the House of Assembly.

Government has been issuing an increasing number of special warrants in recent years, many of which have been issued during March, the last month of the fiscal year. Figure 1 provides information on special warrants issued over the past seven years.



### 3.4 Special Warrants

Figure 1

#### Special Warrants Years Ended 31 March

| Year   | Total number of<br>Special Warrants | Total Special<br>Warrants | Special Warrants<br>Issued in March of<br>each Year |
|--------|-------------------------------------|---------------------------|-----------------------------------------------------|
| 1993   | 7                                   | \$42,360,000              | \$2,500,000                                         |
| 1994   | 2                                   | 40,000,000                | 3,500,000                                           |
| 1995   | 13                                  | 57,855,000                | 30,381,700                                          |
| 1996   | 10                                  | 32,516,000                | 4,100,000                                           |
| 1997   | 7                                   | 75,700,000                | 75,700,000                                          |
| 1998   | 13                                  | 88,601,000                | 34,567,000                                          |
| 1999   | 14                                  | 136,051,900               | 123,824,000                                         |
| Totals | 66                                  | \$473,083,900             | \$274,572,700                                       |

Source: Public Accounts

#### Findings

As Figure 1 indicates, there were 14 special warrants totalling \$136.1 million issued in the 1998-99 fiscal year, of which \$123.8 million were issued in March 1999. Figure 2 provides information on each of these special warrants and indicates that \$95 million of the \$136.1 million were, in my opinion, issued in contravention of the *Financial Administration Act* in that they were not urgently required.

### 3.4 Special Warrants

Figure 2

#### Special Warrants by Department Year Ended 31 March 1999

| Date of Special Warrant | Department                       | Details                                                                                                                                                                                                                                                      | Total         | No Urgent Requirement  |
|-------------------------|----------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------|------------------------|
| 23 Sep. '98             | Forest Resources and Agrifoods   | Emergency fire suppression overruns                                                                                                                                                                                                                          | \$1,028,600   |                        |
| 19 Jan. '99             | Legislature                      | Funding to hold a general election.                                                                                                                                                                                                                          | 3,199,300     |                        |
| 24 Feb. '99             | Human Resources and Employment   | To cover the Province's share of annuity contracts as per the Fisheries Early Retirement Agreement.                                                                                                                                                          | 8,000,000     |                        |
| 12 Mar. '99             | Human Resources and Employment   | To cover the Province's share of annuity contracts as per the Fisheries Early Retirement Agreement.                                                                                                                                                          | 6,900,000     |                        |
| 12 Mar. '99             | Forest Resources and Agrifoods   | Grant - Newfoundland and Labrador Legacy Nature Trust.                                                                                                                                                                                                       | 1,000,000     | \$1,000,000            |
| 12 Mar. '99             | Finance                          | Grant - Newfoundland Municipal Financing Corporation for municipal debt relief.                                                                                                                                                                              | 5,000,000     | 5,000,000              |
| 12 Mar. '99             | Tourism Culture and Recreation   | Grant - Special Celebrations Corporation \$3,300,000<br>Grant - 1999 Corner Brook Winter Games \$500,000                                                                                                                                                     | 3,800,000     | 3,800,000              |
| 12 Mar. '99             | Education                        | Grant - Teaching Services \$14,880,400<br>Grant - School Board Operations \$619,600<br>Grant - Newfoundland and Labrador Education Investment Corporation \$13,650,000<br>Grant - MUN Opportunity Fund \$2,000,000<br>Grant - The Literacy Council \$500,000 | 31,650,000    | 13,650,000<br>500,000  |
| 12 Mar. '99             | Municipal and Provincial Affairs | To cover flooding costs on the Baie Verte Peninsula and central areas of the Province.                                                                                                                                                                       | 1,300,000     |                        |
| 12 Mar. '99             | Health and Community Services    | Grant - Health Care Facilities \$42,500,000<br>Grant - Health Care Facilities - Property Furnishings and Equipment \$16,000,000                                                                                                                              | 58,500,000    | 58,500,000             |
| 31 Mar. '99             | Health and Community Services    | Grant - Health Care Capital Equipment                                                                                                                                                                                                                        | 5,000,000     | 5,000,000              |
| 31 Mar. '99             | Health and Community Services    | Drug Subsidization Program \$2,700,000<br>Grant - Medical Care Commission \$1,600,000<br>Grant - Community Service \$4,300,000                                                                                                                               | 8,600,000     | 1,600,000<br>4,300,000 |
| 31 Mar. '99             | Education                        | Grant - School Board Operations \$1,200,000<br>Grant - Provincial Information and Library Resources Board \$499,000                                                                                                                                          | 1,699,000     | 1,699,000              |
| 31 Mar. '99             | Justice                          | To cover shortfall in Professional Services - Civil Law                                                                                                                                                                                                      | 375,000       |                        |
|                         | Total Special Warrants           |                                                                                                                                                                                                                                                              | \$136,051,900 | \$95,049,000           |

Source: 1998-99 Special Warrants

### 3.4 Special Warrants

**Figure 1**

**Special Warrants  
Years Ended 31 March**

| Year   | Total number of<br>Special Warrants | Total Special<br>Warrants | Special Warrants<br>Issued in March of<br>each Year |
|--------|-------------------------------------|---------------------------|-----------------------------------------------------|
| 1993   | 7                                   | \$42,360,000              | \$2,500,000                                         |
| 1994   | 2                                   | 40,000,000                | 3,500,000                                           |
| 1995   | 13                                  | 57,855,000                | 30,381,700                                          |
| 1996   | 10                                  | 32,516,000                | 4,100,000                                           |
| 1997   | 7                                   | 75,700,000                | 75,700,000                                          |
| 1998   | 13                                  | 88,601,000                | 34,567,000                                          |
| 1999   | 14                                  | 136,051,900               | 123,824,000                                         |
| Totals | 66                                  | \$473,083,900             | \$274,572,700                                       |

Source: Public Accounts

### Findings

As Figure 1 indicates, there were 14 special warrants totalling \$136.1 million issued in the 1998-99 fiscal year, of which \$123.8 million were issued in March 1999. Figure 2 provides information on each of these special warrants and indicates that \$95 million of the \$136.1 million were, in my opinion, issued in contravention of the *Financial Administration Act* in that they were not urgently required.

### 3.4 Special Warrants

Figure 2

#### Special Warrants by Department Year Ended 31 March 1999

| Date of Special Warrant | Department                       | Details                                                                                                                                                                                                                                                      | Total         | No Urgent Requirement  |
|-------------------------|----------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------|------------------------|
| 23 Sep. '98             | Forest Resources and Agrifoods   | Emergency fire suppression overruns                                                                                                                                                                                                                          | \$1,028,600   |                        |
| 19 Jan. '99             | Legislature                      | Funding to hold a general election.                                                                                                                                                                                                                          | 3,199,300     |                        |
| 24 Feb. '99             | Human Resources and Employment   | To cover the Province's share of annuity contracts as per the Fisheries Early Retirement Agreement.                                                                                                                                                          | 8,000,000     |                        |
| 12 Mar. '99             | Human Resources and Employment   | To cover the Province's share of annuity contracts as per the Fisheries Early Retirement Agreement.                                                                                                                                                          | 6,900,000     |                        |
| 12 Mar. '99             | Forest Resources and Agrifoods   | Grant - Newfoundland and Labrador Legacy Nature Trust.                                                                                                                                                                                                       | 1,000,000     | \$1,000,000            |
| 12 Mar. '99             | Finance                          | Grant - Newfoundland Municipal Financing Corporation for municipal debt relief.                                                                                                                                                                              | 5,000,000     | 5,000,000              |
| 12 Mar. '99             | Tourism Culture and Recreation   | Grant - Special Celebrations Corporation \$3,300,000<br>Grant - 1999 Comer Brook Winter Games \$500,000                                                                                                                                                      | 3,800,000     | 3,800,000              |
| 12 Mar. '99             | Education                        | Grant - Teaching Services \$14,880,400<br>Grant - School Board Operations \$619,600<br>Grant - Newfoundland and Labrador Education Investment Corporation \$13,650,000<br>Grant - MUN Opportunity Fund \$2,000,000<br>Grant - The Literacy Council \$500,000 | 31,650,000    | 13,650,000<br>500,000  |
| 12 Mar. '99             | Municipal and Provincial Affairs | To cover flooding costs on the Baie Verte Peninsula and central areas of the Province.                                                                                                                                                                       | 1,300,000     |                        |
| 12 Mar. '99             | Health and Community Services    | Grant - Health Care Facilities \$42,500,000<br>Grant - Health Care Facilities - Property Furnishings and Equipment \$16,000,000                                                                                                                              | 58,500,000    | 58,500,000             |
| 31 Mar. '99             | Health and Community Services    | Grant - Health Care Capital Equipment                                                                                                                                                                                                                        | 5,000,000     | 5,000,000              |
| 31 Mar. '99             | Health and Community Services    | Drug Subsidization Program \$2,700,000<br>Grant - Medical Care Commission \$1,600,000<br>Grant - Community Service \$4,300,000                                                                                                                               | 8,600,000     | 1,600,000<br>4,300,000 |
| 31 Mar. '99             | Education                        | Grant - School Board Operations \$1,200,000<br>Grant - Provincial Information and Library Resources Board \$499,000                                                                                                                                          | 1,699,000     | 1,699,000              |
| 31 Mar. '99             | Justice                          | To cover shortfall in Professional Services - Civil Law                                                                                                                                                                                                      | 375,000       |                        |
|                         | Total Special Warrants           |                                                                                                                                                                                                                                                              | \$136,051,900 | \$95,049,000           |

Source: 1998-99 Special Warrants

### 3.4 Special Warrants

Of the fourteen special warrants issued during the year ended 31 March 1999, nine totalling \$119.4 million were tabled in the Legislature on 30 March 1999 and four totalling \$15.7 million were tabled on 1 April 1999 in accordance with the requirements of the *Financial Administration Act*. The remaining \$1 million special warrant was tabled in the Legislature on 16 November 1998. All special warrants issued were included in the next ensuing *Supplementary Supply Act*, which was presented to the Legislature and approved on 27 May 1999.

#### **Nature of Funding Provided Under Special Warrants**

Of the \$136.1 million in special warrants issued in 1998-99, special warrants totalling \$95 million, as outlined in Figure 2 were, in my opinion, issued in contravention of the *Financial Administration Act*. My opinion is based on a review of the circumstances surrounding the issuance of the \$95 million in special warrants. We identified delays between the date on which the special warrants were authorized, the dates that the cheques were issued, the dates the cheques were cashed and the dates that the funding was used. Since, in my opinion, the funding was not urgently required, it should have been included in the 1999-00 budget. As a result, these special warrants, in my opinion, were not issued in accordance with the requirements of the *Financial Administration Act* which requires that there must be an urgent requirement for the funding.

As an alternative to special warrants, Government could request that the Legislature approve supplementary supply for the introduction of new programs and the provision of unforeseen items prior to the expenditures being incurred. This would be a practical alternative since the House of Assembly is usually in session during March when most of the special warrants in recent years have been issued. The approval of a *Supplementary Supply Act* by the Legislature is consistent with the principle that parliamentary debate should occur before an expenditure is made. This would eliminate the present routine use of special warrants for expenditures which cannot truly be described as urgent.

Details relating to these special warrants totalling \$95 million are as follows:

- **The Department of Forest Resources and Agrifoods**

On 12 March 1999, the Department received authority to pay the Newfoundland and Labrador Legacy Nature Trust a grant of \$1 million. The announcement of the establishment of the Trust was made by the Minister of Forest Resources and Agrifoods on 22 March 1999. The announcement stated that the \$1 million provided by Government is intended to fund the basic operations of the Trust over the first five years or so, and that the Trust will be permitted to draw down the funds at a maximum rate of \$200,000



### 3.4 Special Warrants

per year. However, the Newfoundland and Labrador Legacy Nature Trust was not created until 14 September 1999. Since the Newfoundland and Labrador Legacy Nature Trust did not exist at the time the special warrant was issued, there was no urgent requirement for the \$1 million funding.

- **The Department of Finance**

On 12 March 1999, the Department of Finance was authorized to pay the Newfoundland Municipal Financing Corporation a grant of \$5 million. After receiving the \$5 million grant, the Corporation's reserve fund had a balance of \$10.9 million as at 31 March 1999. Since the Corporation did not use or require the \$5 million approved by special warrant on 12 March 1999 during the 1998-99 fiscal year, there was no urgent requirement for the \$5 million. Records at the Department further indicated that up to 31 July 1999, the balance of the reserve fund was \$9 million, significantly in excess of the \$5 million special warrant. Therefore, I conclude that there was no urgent requirement for the \$5 million special warrant.

- **The Department of Tourism, Culture and Recreation**

On 12 March 1999, the Department of Tourism, Culture and Recreation received authority to pay tourism and recreation grants of \$3.8 million. Of the \$3.8 million in special warrants, \$3.3 million was paid to the Special Celebrations Corporation of Newfoundland and Labrador Inc. and \$500,000 was paid to the 1999 Corner Brook Winter Games Host Society Inc.

Although the Special Celebrations Corporation of Newfoundland and Labrador Inc. received funding that was urgently required, by way of special warrant, during the 1998-99 fiscal year, the financial statements of the Corporation indicated that it did not use the \$3.3 million during the 1998-99 fiscal year. In addition, our review of the bank statements of the Corporation indicated that as at 31 May 1999 the Corporation had a total balance in its two current accounts of \$3,328,196. This is in excess of the \$3.3 million special warrant. Therefore, there was no urgent requirement for the \$3.3 million approved by special warrant for the 1998-99 fiscal year.

The 1999 Corner Brook Winter Games Host Society Inc. received \$500,000. Although the special warrant was approved 12 March 1999, a cheque for the \$500,000 was not issued until 31 March 1999, and was not cashed until 22 April 1999. Therefore, I conclude that there was no urgent requirement for this \$500,000 special warrant.

### 3.4 Special Warrants

- **The Department of Health and Community Services**

The Department of Health and Community Services was authorized to pay \$58.5 million on 12 March 1999 and \$5 million, \$1.6 million and \$4.3 million on 31 March 1999 for a total of \$69.4 million. Details relating to these payments follow:

- On 12 March 1999, a special warrant for \$58.5 million was approved. The \$58.5 million was issued through 25 cheques to the Health Care Boards. The first cheque for \$5 million was issued on 31 March 1999, 19 days after the date of the special warrant. The remaining 24 cheques were not issued until April and May of 1999, the earliest on 7 April 1999. Therefore, I conclude that there was no urgent requirement for the \$58.5 million special warrant.
- On 31 March 1999, a special warrant for \$5 million was approved. This represented the department's contribution towards costs associated with the year 2000 computer issues. Although the \$5 million was paid on 31 March 1999, it was not deposited until 7 April 1999. Therefore, this expenditure could have been provided for in the 1999-2000 budget. As a result, I conclude that there was no urgent requirement for the \$5 million special warrant.
- A grant of \$1.6 million was paid to the Newfoundland Medical Care Commission for physician services. Although the funding was approved by special warrant on 31 March 1999, the \$1.6 million was not paid out until 27 April 1999. Therefore, I conclude that there was no urgent requirement for the \$1.6 million special warrant.
- Grants totalling \$4.3 million were paid to the four Health and Community Services Boards, the Grenfell Regional Health Services Board and the Health Labrador Corporation for social programs.

Although the funding was approved by special warrant on 31 March 1999, the \$4.3 million was not paid out until 23 April 1999. Therefore, I conclude that there was no urgent requirement for the \$4.3 million special warrant on 31 March 1999.

- **The Department of Education**

The Department of Education was authorized to pay \$13.7 million and \$500,000 on 12 March 1999 and \$1.7 million on 31 March 1999 for a total of \$15.9 million. Details relating to these payments follow:

### 3.4 Special Warrants

- A grant of \$13.7 million was approved by special warrant on 12 March 1999 for the Newfoundland and Labrador Education Investment Corporation. However, as at 31 March 1999, the Corporation had investments of approximately \$36 million which included the \$13.7 million. Records at the Department indicated that as at 28 October 1999, it still had investments totalling \$19.6 million, significantly in excess of the \$13.7 million special warrant. Therefore, I conclude that there was no urgent requirement for the \$13.7 million approved by special warrant.
- On 31 March 1999, \$1.2 million was approved by special warrant for five school boards relating to operating deficits. Five cheques totalling \$1,186,100 were dated 16 April 1999. However, four cheques totalling \$686,800 were not deposited until 29 July 1999, 3 August 1999, 3 August 1999 and 4 August 1999. The remaining cheque for \$499,300 was still in a filing cabinet at the Department of Education at the time of our review in September 1999. Subsequent to our enquiry, the cheque dated 16 April 1999 for \$499,300 was cancelled and re-issued on 17 September 1999. This cheque was subsequently deposited on 30 September 1999. Therefore, I conclude that there was no urgent requirement for the \$1.2 million special warrant.
- A grant of \$500,000 to the Literacy Council was approved by a special warrant on 12 March 1999. The cheque was issued on 12 April 1999 and was cashed on 14 April 1999. On 28 April 1999, the Department instructed the Literacy Council not to disburse these funds until further direction was received from the Department. Since the cheque was not issued until the 1999-00 fiscal year and the Department did not know what the funds would be used for, I conclude that there was no urgent requirement for a special warrant on 12 March 1999.
- A grant of \$499,000 was approved by special warrant on 31 March 1999 to the Provincial Information and Library Resources Board. The cheque was issued on 12 April 1999 and was cashed on 14 April 1999. On 28 April 1999, the Department instructed the Board not to disburse these funds until further direction was received from the Department. Since the cheque was not issued until the 1999-00 fiscal year and the Department did not know what the funds would be used for, I conclude that there was no urgent requirement for a special warrant on 31 March 1999.



### 3.4 Special Warrants

#### Impact on Government's Financial Results

Figure 3 clearly shows that since the 1992-93 fiscal year, Government's actual cash surplus or deficit before special warrants was always more favourable than the cash surplus or deficit projected in the cash budget which was approved by the House of Assembly.

After issuing special warrants in each of these 7 years, Government reduced its cash surplus or increased its cash deficit. As Figure 3 shows, the use of special warrants provides Government with the flexibility to "adjust" the cash surplus or deficit and produce a result closer to that originally budgeted on the cash basis.

It is my opinion that \$95 million of the \$136.1 million of the special warrants issued in 1998-99 did not meet the requirements of the *Financial Administration Act* in that they were not urgently required and therefore should not have been issued. If these special warrants had not been issued, and in my opinion they should not have been, Government would have reported a cash surplus of \$105.1 million compared to the \$10.1 million that was actually reported.

Figure 3

#### Reported Deficits/Surpluses Years Ended 31 March (000's)

| Year | Cash<br>Deficit/Surplus<br>Projected in the<br>Budget | Cash<br>Surplus/Deficit<br>Before Special<br>Warrant | Special<br>Warrants | Cash<br>Surplus/Deficit<br>After Special<br>Warrants |
|------|-------------------------------------------------------|------------------------------------------------------|---------------------|------------------------------------------------------|
| 1993 | \$ (239,734)                                          | \$ (200,091)                                         | \$ 42,360           | \$ (242,451)                                         |
| 1994 | (223,256)                                             | (154,036)                                            | 40,000              | (194,036)                                            |
| 1995 | (196,671)                                             | (63,148)                                             | 57,855              | (121,003)                                            |
| 1996 | 1,944                                                 | 38,368                                               | 32,516              | 5,852                                                |
| 1997 | (44,772)                                              | 54,547                                               | 75,700              | (21,153)                                             |
| 1998 | (20,311)                                              | 77,680                                               | 88,601              | (10,921)                                             |
| 1999 | (9,987)                                               | 146,112                                              | 136,051             | 10,061                                               |

Source: Public Accounts and Budget

### 3.4 Special Warrants

#### Treasury Board Secretariat's Response

*I offer the following comments for your consideration.*

- *The Legislature has granted authority to Government to issue Special Warrants when certain circumstances are met. This authority is clearly outlined in the Financial Administration Act. In each case where a Special Warrant is issued, the relevant Minister must provide a statement indicating that the need for the Special Warrant is urgent. In addition, the Legislation requires, through the Financial Administration Act, that Government table Special Warrants in the Legislature within certain time frames.*

*The need for Special Warrants will inevitably arise from time to time, and a review of our records indicates that Special Warrants have, in fact, been issued in most years.*

- *You have indicated that in recent years an increasing number of Special Warrants were issued, many of which were in March, the last month of the fiscal year. It must be recognized that our financial condition is subject to a high degree of dependence on federal transfer payments. These transfer payments are by their nature, highly volatile. Given higher revenues than expected towards year end, Government has utilized the Special Warrants mechanism to make some expenditures that they felt served the public good. This was in an effort to avail of the year-end flexibility and provide for a stable financial performance.*
- *A number of your comments make the claim that, in your opinion, the need for certain of the expenditures authorized by Special Warrants was not urgent. The Financial Administration Act does not define or qualify what should constitute urgency. In all cases appropriate statements as to urgency had been prepared by Ministers, and were tabled in the House of Assembly, as required by the Act.*

*I am not aware of any guidelines that would be helpful in determining what would constitute an urgent requirement. Presumably, in this case, the appropriate Ministers felt there was an urgency, and the House of Assembly obviously concurred. Accordingly, I believe that the Special Warrants meet the requirements of the Financial Administration Act.*

### 3.4 Special Warrants

- *In addition, the payments relating to the appropriations authorized by the Special Warrants were properly accounted for in the Consolidated Revenue Fund. The deficit reported in the Consolidated Summary Financial Statements is not affected by any amounts unexpended in the applicable Crown Entities. This is because of the consolidation process.*

### **3.5 Cellular Phones in Government**

#### **Introduction**

Government is required to communicate across a large geographical area comprised of both accessible and remote locations and uses a variety of modes to meet its telecommunication needs. Prior to 1991, mobile radios and pagers were generally used by Government to meet the communication needs of the Province. The mobile systems were particularly effective in outlying areas and pagers were prominent in the immediate locality of the Government offices. Around 1991, the cellular phone, promoted as a more practical alternative, began to replace, where possible, the existing equipment. Since the use of cellular phones is increasing, government should ensure adequate systems and procedures are in place.

#### **Scope and Objectives**

We completed our review of the acquisition and administration of cellular phones in June 1999. Our objective was to determine whether there were policies in place to control the acquisition and administration of cellular phones.

#### **Conclusions**

Many Government departments do not have adequate control over the acquisition and administration of cellular phones, and not all departments have developed procedures to verify receipt of cellular service and approve invoices for payment. For example:

- Many departmental records of cellular phones are incomplete and inaccurate.
- Some departments are paying for cellular phones that are not in use.
- There was no indication at many departments that all invoices were reviewed by employees to verify cellular phone calls, that invoices were approved by the directors responsible, and that unusual calls were investigated.

#### **Findings and Recommendation**

Government has policies that govern the acquisition and installation of standard desk telephones and the verification, certification and approval of telephone charges. This enables Government to control installations and payment for telephone services. Also, these telephones are controlled by the serial number, telephone number and the individual to whom the telephone is assigned. In addition, the responsibility for the acquisition and the installation of telephones and the maintenance of the inventory resides in the Department of Works, Services and Transportation.

### **3.5 Cellular Phones in Government**

For the acquisition of cellular phones, we expected to see similar policies which would indicate how the service package should be selected, whether the phone can be used for personal calls and whether the cellular phone is stationary (i.e. permanently resides in that department) or transferrable (i.e. moves with the employee if they move from the department). In the absence of policies, departments cannot adequately monitor and control cellular phones.

Our review indicated that there is no government wide policy for the acquisition and administration of cellular telephones. As a result, on 6 May 1999 we requested 18 departments provide us with a copy of their departmental policies related to cellular phones, as well as their listing of departmental cell phone numbers. Three departments provided a copy of their policy on cellular phones, 7 departments responded that they did not have a separate policy but used government's general purchasing and payment policies, while the remaining 8 departments had no policy. Furthermore, departments cannot readily determine the cost of cellular telephones as they do not accumulate these costs in a separate account in Government's accounting system.

#### **Acquisition and Inventory**

Since there is no central management of the acquisition, activation and maintenance of inventory records for cellular telephones as there is for desk telephones, we interviewed the directors of 10 divisions in 8 government departments to obtain an overview of the manner in which cellular telephones are managed. We found the common procedure required an employee, who determined they required a cellular telephone to complete their duties, to obtain the approval of their director prior to acquisition of a cellular telephone. Once approved, the cellular service package was chosen based on the needs of the position and the cost, with reference to the standing offer agreement for the purchase of cellular service.

The directors also informed us that invoices for service are initially received and verified by the employees in the divisions. All directors, or a designated individual in the division, perform some level of analysis on the invoices which range from scanning the invoices for reasonableness to examination of time, location and numbers called. Calls to unfamiliar numbers not verified by employees are returned for an explanation. The directors of all divisions we visited indicated they approved the invoices for payment. We examined invoices on a test basis to establish whether there was evidence that the review and approval procedures were functioning. Our review indicated that in many departments there was no indication that all invoices were reviewed by employees to verify cellular phone calls, that invoices were approved by the directors responsible, and that unusual calls were investigated.

### 3.5 Cellular Phones in Government

In addition to the cellular telephone listings obtained from the 18 departments, we obtained the invoices for March 1999 and compared the invoices to the cellular phone listings to determine whether these listings were complete and accurate and whether departments were paying only for services it received. Our review identified many valid government cell phone numbers which were not included in the departmental listings and some departments paid for cellular telephones after they were requested for disconnection. As a result, we concluded that government does not have adequate control over cellular telephones. A summary, by department, of the results of our review, is outlined in Figure 1.

**Figure 1**

#### Summary of Exceptions Cellular Telephones in Government March 1999

| Department                         | Phone listing complete | Do all phone numbers on listing belong to the Department | Are all phones on listing in use | Bills paid only for phones in use | Number of cellular phones |
|------------------------------------|------------------------|----------------------------------------------------------|----------------------------------|-----------------------------------|---------------------------|
| Industry, Trade and Technology     | No                     | Yes                                                      | Yes                              | No                                | 29                        |
| Tourism, Culture and Recreation    | No                     | No                                                       | No                               | Yes                               | 46                        |
| Environment and Labour             | No                     | No                                                       | No                               | No                                | 35                        |
| Municipal and Provincial Affairs   | No                     | Yes                                                      | Yes                              | Yes                               | 25                        |
| Government Services and Lands      | Yes                    | Yes                                                      | Yes                              | Yes                               | 28                        |
| Development and Rural Renewal      | Yes                    | Yes                                                      | Yes                              | Yes                               | 11                        |
| Works, Services and Transportation | No                     | Yes                                                      | Yes                              | Yes                               | 177                       |
| Forest Resources and Agrifoods     | No                     | No                                                       | No                               | Yes                               | 123                       |
| Mines and Energy                   | Yes                    | Yes                                                      | Yes                              | Yes                               | 25                        |
| Fisheries and Aquaculture          | No                     | Yes                                                      | Yes                              | Yes                               | 43                        |
| Executive Council                  | No                     | Yes                                                      | Yes                              | Yes                               | 40                        |
| Public Service Commission          | Yes                    | Yes                                                      | Yes                              | Yes                               | 6                         |
| Finance                            | Yes                    | Yes                                                      | Yes                              | Yes                               | 6                         |
| Legislature                        | Yes                    | Yes                                                      | Yes                              | Yes                               | 5                         |
| Education                          | No                     | Yes                                                      | Yes                              | No                                | 15                        |
| Health and Community Services      | Yes                    | Yes                                                      | Yes                              | Yes                               | 6                         |
| Justice                            | No                     | Yes                                                      | Yes                              | Yes                               | 41                        |
| Human Resources and Employment     | No                     | Yes                                                      | Yes                              | Yes                               | 34                        |
|                                    |                        |                                                          |                                  | <b>Total</b>                      | <b>695</b>                |

Source: Departmental inventory listings



### 3.5 Cellular Phones in Government

#### **Recommendations**

*Given the increasing costs of cellular telephone service, Government should approve a policy on the acquisition and administration of cellular telephones, and instruct Government departments to charge the cost of cellular telephones to a separate account.*

*Given the increasing number of cellular telephones, Government should prepare and issue a cellular telephone directory listing.*

#### **Treasury Board Secretariat's Response**

*As is the case with all equipment and the processing of invoices for payment, departments are required to maintain accurate inventory records and to follow the appropriate review approvals and certification procedures. It is my understanding that you have corresponded with departments with respect to the accuracy of their inventory records and related administration matters generally noted in your report.*

*Treasury Board Secretariat will consider your recommendations with respect to the development of appropriate policies related to the acquisition, administration and accounting for cellular telephones. We will also contact the Department of Works, Services and Transportation with respect to considering the issuance of a cellular telephone directory listing.*



### 3.6 Accounts and Loans Receivable in Government

#### Introduction

As I have indicated in previous reports to the House of Assembly, Government's systems for recording, reporting and controlling accounts receivable do not always provide timely and accurate information to users. As a result, Government does not know how much money is owed to it at any given point in time. The general exception is the amount owed as of the 31 March of each year which is determined subsequent to year end in order to prepare the financial statements of the Province. Government anticipates that this problem will be addressed with the implementation of its new accounting system. I note that Government introduced the accounts receivable function of its new accounting system in May 1999 and between May and October 1999 the accounts receivable function was implemented in 12 of the 15 departments.

Our review of Government departments also indicates that a significant portion of their accounts receivable are in arrears and that their cash management program, which includes the collection of these accounts, is not adequate.

Figure 1 provides information on amounts owed to Government for each of the seven years to 31 March 1999 along with the amount that Government considers to be uncollectible and amounts written off. These amounts owed include accounts and taxes receivable, as well as loans, advances and mortgages receivable.

**Figure 1**

**Consolidated Revenue Fund  
Accounts, Taxes, Loans, Advances and  
Mortgages Receivable  
Years Ended 31 March  
(\$000's)**

|                                                    | 1993      | 1994      | 1995      | 1996      | 1997      | 1998      | 1999      | Total     |
|----------------------------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Total Receivables                                  | \$531,265 | \$544,156 | \$551,764 | \$537,153 | \$474,797 | \$461,612 | \$471,466 |           |
| Less: Amounts<br>Considered to be<br>Uncollectible | 242,480   | 255,565   | 279,065   | 279,924   | 215,210   | 211,832   | 242,344   |           |
| Net Receivables                                    | \$288,785 | \$288,591 | \$272,699 | \$257,229 | \$259,587 | \$249,780 | \$229,122 |           |
| Amounts Written-off                                | \$80,022  | \$14,242  | \$5,398   | \$20,790  | \$69,877  | \$7,972   | \$1,855   | \$200,156 |

Source: Consolidated Revenue Fund Financial Statements

### 3.6 Accounts and Loans Receivable in Government

#### Scope and Objectives

We reviewed the amounts owed to Government as at 31 March 1999 to determine whether they are collected on a timely basis.

#### Conclusion

In addition to not collecting amounts owed to it on a timely basis, Government has written off significant amounts owed to it.

#### Findings and Recommendation

Figure 2 provides details on the \$471.5 million owed to Government as of 31 March 1999:

Figure 2

**Consolidated Revenue Fund  
Amounts owed to Government  
31 March 1999  
(\$000's)**

| Type of Receivable             | Balance               | Amount Outstanding in Excess of One Year | Amount Considered Doubtful of Collection |
|--------------------------------|-----------------------|------------------------------------------|------------------------------------------|
| Crown Agencies                 | (Note 1)<br>\$224,187 | \$26,050                                 | \$131,122                                |
| Taxes receivable               | 121,062               | 51,303                                   | 48,246                                   |
| Commercial loans               | 31,656                | 19,527                                   | 28,240                                   |
| Miscellaneous receivables      | 41,373                | 10,970                                   | 4,891                                    |
| Court fines                    | 23,114                | 17,235                                   | 11,255                                   |
| Social Assistance overpayments | 26,887                | 22,635                                   | 17,312                                   |
| Other                          | 3,187                 | 390                                      | 1,278                                    |
| <b>Total</b>                   | <b>\$471,466</b>      | <b>\$148,110</b>                         | <b>\$242,344</b>                         |

Note 1 Of the \$224.2 million relating to Crown Agencies, \$134.5 million relates to Enterprise Newfoundland and Labrador Corporation, the Fisheries Loan Board of Newfoundland and the Farm Development Loan Board. The amount owed to these entities for loans made is \$47.8 million in arrears. Also, of the \$224.2 million, \$31.3 million is owed by the Newfoundland Industrial Development Corporation on a long-term basis with no specific repayment date.

### 3.6 Accounts and Loans Receivable in Government

Our review of the amount owed to Government indicated the following:

- Government's average cost of borrowing in the capital market for the year ended 31 March 1999 was 5.99%. If Government had collected the \$148.1 million outstanding for more than one year and the \$47.8 million in arrears with the lending entities and used these funds to retire debt or to reduce current borrowing, annualized savings on debt servicing could have exceeded \$11.7 million.

During the last seven years Government has written off \$200 million in accounts receivable owed to it as follows:

**Figure 3**

**Consolidated Revenue Fund  
Accounts and Loans Receivable Written Off  
1993 to 1999  
(\$000's)**

| Entity                                                                                | Amount   |
|---------------------------------------------------------------------------------------|----------|
| Baie Verte Mines Inc.                                                                 | \$47,551 |
| Newfoundland Industrial Development Corporation                                       | 29,229   |
| Newfoundland Enviroponics Limited                                                     | 15,252   |
| Newco Corporations                                                                    | 15,361   |
| Enterprise Newfoundland and Labrador                                                  | 10,894   |
| Newfoundland Dockyard                                                                 | 8,065    |
| Ocean Harvesters Limited                                                              | 6,649    |
| Cape Pine Fisheries Ltd.                                                              | 6,466    |
| Fisheries Loan Board of Newfoundland                                                  | 4,421    |
| Miscellaneous Loans and Mortgages Forgiven which are less than \$300,000 individually | 4,097    |
| Court Fines                                                                           | 3,938    |
| St. Lawrence Fluorspar Limited                                                        | 3,919    |
| Fisheries Loans                                                                       | 3,849    |
| Social Assistance Overpayments                                                        | 3,802    |
| Notre Dame Bay Fisheries                                                              | 3,762    |
| Universal Group of Companies                                                          | 3,504    |
| Department of Health                                                                  | 3,339    |



### 3.6 Accounts and Loans Receivable in Government

Figure 3 (cont'd)

| Entity                                                            | Amount           |
|-------------------------------------------------------------------|------------------|
| Harbour Grace Fishing Company Limited                             | 2,368            |
| Oceana Seafood Processors Limited                                 | 2,175            |
| St. Clares Mercy Hospital                                         | 1,993            |
| Other Government Departments - Accounts Written Off               | 1,645            |
| Superior Seafoods Limited                                         | 1,567            |
| St. John's Metropolitan Area Board                                | 1,475            |
| Governor's Park Limited                                           | 1,428            |
| Great Northern Seafoods Limited                                   | 1,414            |
| Petty Harbour Fishermen's Producer's Co-operative Society Limited | 1,316            |
| Blue Ocean Products Limited                                       | 1,314            |
| Gander Masonic Memorial Complex                                   | 1,240            |
| Reid's Products Limited                                           | 931              |
| Petty Harbour Fisheries Ltd.                                      | 926              |
| Belle Isle Seafoods Ltd.                                          | 799              |
| S.T. Jones and Son Limited                                        | 795              |
| White's Fisheries Limited                                         | 770              |
| Department of Natural Resources                                   | 667              |
| Island Tile and Slate                                             | 513              |
| Nordco Limited                                                    | 478              |
| Department of Fisheries                                           | 469              |
| Reg Petten                                                        | 465              |
| Sop's Arm Fisheries (1988) Limited                                | 341              |
| Ocean Kist Products (1970) Ltd.                                   | 338              |
| Department of Works, Services and Transportation                  | 316              |
| Trouty Seafoods Limited                                           | 315              |
| <b>Total</b>                                                      | <b>\$200,156</b> |

### 3.6 Accounts and Loans Receivable in Government

Figure 3 (cont'd)

| Entity                                                            | Amount           |
|-------------------------------------------------------------------|------------------|
| Harbour Grace Fishing Company Limited                             | 2,368            |
| Oceana Seafood Processors Limited                                 | 2,175            |
| St. Clares Mercy Hospital                                         | 1,993            |
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| Department of Natural Resources                                   | 667              |
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| Reg Petten                                                        | 465              |
| Sop's Arm Fisheries (1988) Limited                                | 341              |
| Ocean Kist Products (1970) Ltd.                                   | 338              |
| Department of Works, Services and Transportation                  | 316              |
| Trouty Seafoods Limited                                           | 315              |
| <b>Total</b>                                                      | <b>\$200,156</b> |



### 3.6 Accounts and Loans Receivable in Government

- In addition to the \$200.2 million, during the years 1993 to 1999 the Province wrote off \$11.3 million in tax forgiveness and \$19.5 million in tax remissions.
- As at 31 March 1999, Government anticipated that \$242.3 million or 51.4% of the \$471.5 million amount owed to it will likely not be collected.
- Prior to May 1999 there was no Government-wide system to record, control and collect total amounts owed to Government. Departmental systems ranged from manual year-end listings and other manual records, to computerized systems and there was little consistency among those systems. In May 1999 Government introduced the accounts receivable function of its new accounting system. Government anticipates that this system will address the concerns relating to its system of recording, controlling and monitoring accounts receivable. I am pleased to report that during the period May to October 1999, the new accounts receivable system was implemented in 12 of the 15 departments of Government.

#### Recommendations

*Accounts receivable should be collected on a timely basis.*

*Government should continue to implement its new accounts receivable system so that it can ensure that all amounts owing to it are properly recorded, controlled, monitored and collected on a timely basis.*

#### Treasury Board Secretariat's Response

*I agree with your recommendations. The departments are responsible for the timely collection of accounts receivable and the related management of their accounts. The Treasury Board Secretariat has been active in encouraging improvements in collections and related activities of the departments by sponsoring information sessions, analysis and feedback with respect to write-off requests, routine interaction with departments and provision of advice when requested, etc.*

*Several months ago, a committee was established to focus on government-wide matters related to collections. The committee has representation from the line departments and, as resources are available, will work towards improvements in policies and procedures identified for review.*

*As you had noted, a government-wide accounts receivable system has been implemented to facilitate the management of accounts receivable. The system will be installed in the remaining departments.*



### 3.7 Human Resource Management Information System

#### Introduction

The payment of salaries and benefits for public employees is Government's largest expenditure. Total salaries and benefits, including government departments and Crown agencies, totalled \$1.3 billion in 1998-99 (\$1.2 billion 1997-98). Of this \$1.3 billion, government departments accounted for \$297 million comprised of \$258 million in salaries and \$39 million in employee benefits. Given the magnitude of these expenditures, it is critical that Government have the ability to analyze, monitor and control its human resources and related expenditures.

In 1987, government formally recognized the need to automate all its human resource systems to enable it to effectively manage human resources. At that time human resource information within Government was maintained in a number of main systems as outlined in Figure 1.

The systems outlined in Figure 1 operated independently of each other and also lacked the capability to provide ready access to important information such as employees' education and experience. All of this made it either difficult or impossible to effectively manage Government's human resources.

Figure 1

#### Human Resource Systems 1987

| Government Department              | Human Resource Information                                                                                                                                                                                      |
|------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Finance                            | Payroll system for employees within Government providing information on employees' various earnings and deductions.<br><br>Pension Administration System containing information related to pensionable service. |
| Works, Services and Transportation | Payroll system for certain of the Department's employees.                                                                                                                                                       |
| Forestry                           | Payroll system for certain of the Department's employees.                                                                                                                                                       |
| Treasury Board Secretariat         | Information specific to collective bargaining, classification and compensation, insurance, personnel policy, and salary and position monitoring.                                                                |
| Public Service Commission          | Information specific to recruitment, staff training and development, and other personnel services.                                                                                                              |
| All Government Departments         | Manual and automated systems for employees' attendance and leave records.                                                                                                                                       |

### **3.7 Human Resource Management Information System**

To address these issues and to automate all of its human resource systems, Government established a Steering Committee in 1987 to develop a comprehensive computerized Human Resource Management Information System with implementation scheduled for early 1993 at an estimated cost of \$2.1 million. The human resource management information system project was intended to overcome these shortcomings by integrating the payroll and other human resource systems within Government.

In 1993 we examined human resource management at Treasury Board Secretariat and reported that there was a delay in implementing the planned system. We also reported that existing human resource systems and information in Government were as diverse and incompatible as they were in 1987 when the project started.

In 1994, Government agreed in principle with a single centralized payroll system to administer the compensation budgets of all boards, agencies and commissions and directed Treasury Board to proceed with a feasibility study and development of an implementation plan on a priority basis.

#### **Scope and Objectives**

We completed our review of the development of the Human Resource Management Information System in June 1999. Our objective was to determine what progress has been made since 1987 in developing a human resource management information system.

#### **Conclusions**

As a result of our review we conclude that:

- In 1987 Government recognized the need to more effectively manage its human resources and established a Steering Committee to develop a comprehensive computerized Human Resource Management Information System. In 1990 it was determined that a new system would cost approximately \$2.1 million and would be completed by March 1993. There were 17 functional areas that were identified as necessary to address in order to have the required system. As at 31 March 1995, Government had spent approximately \$4.3 million and no further significant costs have been incurred. At the time of our review, Government had only developed or partially developed 5 of the 17 functional areas and made enhancements to 4 functional areas. Government still does not have an adequate Human Resource Management Information System.

### **3.7 Human Resource Management Information System**

#### **Findings and Recommendations**

##### **1. HRMIS Development**

The Human Resource Management Information System planned in 1987 was intended to provide a comprehensive information system that would capture and report human resource information that could be used to manage Government's human resources and related expenditures.

Based on a thorough analysis of Government's human resource management functions, the resulting Systems Requirements Definition document, dated April 1990, identified 17 areas that needed to be addressed in order to have a system that would provide the information necessary to effectively manage Government's human resources. These 17 areas were ranked as either mandatory, highly desirable or desirable and are outlined in Figure 2.

We reviewed the current status of these 17 areas that needed to be addressed to determine the current status. Figure 2 outlines our findings relating to these 17 areas.

The types of information which would be provided by the 17 functional areas in Figure 2 include the following:

- Tracking of sick leave on a government-wide basis;
- Tracking the number of permanent and temporary employees;
- Tracking employees whose positions are declared redundant and who are subsequently rehired;
- Maintaining demographic information for such areas as succession planning and early retirement options;
- Collective bargaining such as costing of employee benefits and projecting the cost of changes;
- Employee profile including training, education, professional membership and skills;
- Performance appraisals; and
- Overtime administration.

### 3.7 Human Resource Management Information System

Figure 2

**Human Resource Management Information System  
by ranked functional area and development status**

| Functional Area             |                                | Action since 1990   | Departmental access    | Comments                                                                                                                                                                            |
|-----------------------------|--------------------------------|---------------------|------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Considered Mandatory</b> |                                |                     |                        |                                                                                                                                                                                     |
|                             | Position Administration        | Developed           | Inquiry                |                                                                                                                                                                                     |
|                             | Classification                 | Enhanced            | Inquiry                | Additional data captured.                                                                                                                                                           |
|                             | Compensation                   | Enhanced            | Inquiry                | Additional data captured.                                                                                                                                                           |
|                             | Payroll Processing             | Developed           | Data entry and inquiry | Payroll data standardized; however, a separate payroll system maintained by the Department of Works, Services and Transportation was not combined with Government's payroll system. |
|                             | Demographics                   | Enhanced            | Data entry and inquiry | Additional data captured.                                                                                                                                                           |
|                             | Attendance/Leave Management    | No progress         | No access              |                                                                                                                                                                                     |
| <b>Highly Desirable</b>     |                                |                     |                        |                                                                                                                                                                                     |
|                             | Recruitment and Selection      | Developed           | No access              | Separate system developed for use by the Public Service Commission.                                                                                                                 |
|                             | Insurance                      | Developed           | Inquiry                | Manual system automated in Treasury Board Secretariat.                                                                                                                              |
|                             | Staff Training and Development | Partially developed | No access              | Separate system developed for use by the Public Service Commission; however, it does not reflect departmental training initiatives.                                                 |
|                             | Collective Bargaining          | Enhanced            | No access              | Capture of additional data and ad hoc reporting as required.                                                                                                                        |
|                             | Communications                 | No progress         | No access              |                                                                                                                                                                                     |
| <b>Desirable</b>            |                                |                     |                        |                                                                                                                                                                                     |
|                             | Development Opportunities      | No progress         | No access              |                                                                                                                                                                                     |
|                             | Staff Relations                | No progress         | No access              |                                                                                                                                                                                     |
|                             | Employee Services              | No progress         | No access              |                                                                                                                                                                                     |
|                             | Employee Profile               | No progress         | No access              |                                                                                                                                                                                     |
|                             | Health and Safety              | No progress         | No access              |                                                                                                                                                                                     |
|                             | Other Administration           | No progress         | No access              |                                                                                                                                                                                     |

Source: Systems Requirements Definition Document

### 3.7 Human Resource Management Information System

As Figure 2 indicates, five functional areas were developed or partially developed, four functional areas were enhanced and no progress was noted in eight functional areas. While certain functional areas were developed or enhanced, the development or enhancement was not integrated into one system as was originally proposed. The Project Scope Document dated February 1989 envisioned a solution for human resource information where the HRMIS system would be *"a repository of information on positions, employees, and employment. This system would be connected with other specialized systems that provide or require employee information."* The efficiencies from such a system have not been realized due to the fact that, for example, data is duplicated in separate systems and human resource data is not accessible on a government-wide basis.

There was an existing payroll system prior to the HRMIS initiative. This was the Public Service Payroll System which was operated by the Department of Finance and processed payroll for Government departments.

As a result of the HRMIS initiative, Government's existing payroll system was decentralized beginning in January 1995 and Departments were given responsibility for completion of all forms, data entry and data verification. In addition, employees paid by a separate payroll system maintained by the Department of Forestry were transferred to Government's payroll system in 1993. However, employees paid by a separate payroll system maintained by the Department of Works, Services and Transportation also scheduled to be transferred to Government's payroll system were not transferred and that system continues to operate. There are 1,650 employees on this system and the Department spends approximately \$57,500 per year to run and maintain it.

#### 2. HRMIS Expenditure

Expenditure on HRMIS exceeded its budget and planned implementation targets were not met. The Implementation Strategy and Project plan document dated October 1990 contained a budget estimate of \$2.1 million to implement systems for the 17 functional areas outlined in Figure 2. All of this work was scheduled to be completed by 31 March 1993.

Our review indicated that the cumulative cost, excluding the salary cost of seconded employees, incurred for the HRMIS development from 1 April 1988 to the fiscal year ended 31 March 1995 was \$4.3 million and no further significant costs have been incurred. At the time of our review, Government had only developed or partially developed 5 of the 17 functional areas and made enhancements to 4 functional areas.



### **3.7 Human Resource Management Information System**

#### **3. Human Resource Information Management Development Status**

In January 1998, a new initiative was undertaken as a result of public service reform. A Human Resource Information Management Strategy project team was formed with the purpose of developing a strategy aimed at satisfying the human resource information needs of departments, central agencies and other users of Government's human resource information. The project team concluded that many of the major issues identified in 1987 and again in 1990 were still issues and that time had only increased the need to have shortcomings in human resource information management addressed. This project team presented its report to the Public Service Reform Secretariat and the Organizational and Human Resource Management Task Force.

#### **Recommendation**

*Treasury Board Secretariat should implement a comprehensive human resource management information system.*

#### **Treasury Board Secretariat Response**

*The Human Resource Management Information System (HRMIS) project resulted in significant progress in terms of delivery of the human resource management function for government.*

*Prior to HRMIS, government departments operated primarily with a highly clerical, manual paper process of recording payroll and position transactions which were then forwarded and processed centrally at the Department of Finance. As part of the delivery of HRMIS, these processes were standardized, automated and decentralized to departments for data entry and inquiry purposes, with some functions remaining central for purposes of ensuring necessary security and control standards. Additionally, new and enhanced functionality was delivered in many areas which did not previously exist such as Group Insurance Administration, Seniority Administration, Position Administration, Classification Administration, etc.*

*It became evident during the systems development effort that the original estimate of \$2.1 million had to be revised and that not all functional areas could be addressed given the complexity and breadth of human resource information required in Government. As a result of these findings, it was necessary to revise the scope of the project and funding allocated. During the annual budget process, Government approved additional funding based on the revised project plan.*

### **3.7 Human Resource Management Information System**

*Following these efforts, overall Government information technology priorities changed with the focus shifting to non-human resource related areas for a period of time. The Secretariat disagrees with the recommendation to develop a single, comprehensive human resource management information system but it does intend to review and address current day requirements, utilizing a modular approach, as funding permits.*



### **3.8 A Review of the Financial Management System**

#### **Introduction**

In June 1997, Treasury Board Secretariat approved the replacement of Government's existing financial systems. This replacement was necessary as these systems were not Year 2000 compliant and Government felt that further customization of these systems would not be cost effective. In November 1998, Government completed the replacement of these key financial systems with a new integrated Financial Management System. The acquisition and implementation of the new Financial Management System was one of the most significant information technology projects undertaken by Government, involving over 15 departments and 500 users at 31 different locations.

Responsibility for the Financial Management System Project was assigned to the Office of the Comptroller General of the Treasury Board Secretariat. NewTel Information Solutions Limited (NIS -now xwave solutions), as the main provider of information technology services to Government, was contracted to provide project management and professional services for the Project.

In selecting a financial system, a Request for Proposals was not issued due to a number of considerations including what Government considered to be imposed time constraints in implementing a system that would be Year 2000 compliant. To assist in the selection of the new financial system, Government engaged the services of the Gartner Group. The Gartner Group is recognized by Government and NIS as an independent, impartial source of quality knowledge about financial packages. The Gartner Group provided consultative services as well as the software which was used by NIS and Government to select the top two vendors of public sector financial packages. In January 1997, a Request for Information was sent to these two vendors. Responses from the vendors were evaluated jointly by Government and NIS and in February 1997, Oracle was selected as the successful vendor.

The Vendor Recommendation Report, prepared by NIS in evaluating vendor responses to the Request for Information, detailed Oracle's cost projections for the new system at \$13.0 million. Upon selecting Oracle as the successful vendor, Government, NIS and Oracle entered into negotiations to refine project specifications and costs. As a result of these negotiations, implementation of the new system was scheduled to be completed by 5 October 1998 with a project budget of \$7.9 million. Figure 1 provides information on the cost estimates included in the Vendor Recommendation Report and the approved project budget for the acquisition and implementation of the Financial Management System.



### 3.8 A Review of the Financial Management System

Figure 1

#### Financial Management System Estimated Costs (\$ Millions)

| Expenditure Type        | Vendor Recommendation Report | Project Budget |
|-------------------------|------------------------------|----------------|
| Professional Services   |                              |                |
| NIS                     | 7.4                          | 2.3            |
| Oracle and Other        | 2.0                          | 1.4            |
| Government Resources    | -                            | 0.7            |
| Travel                  | 1.0                          | 0.6            |
| Sub-total               | 10.4                         | 5.0            |
| Hardware and Peripheral | 1.4                          | 1.5            |
| Software                | 0.8                          | 0.9            |
| Training                | 0.4                          | 0.3            |
| Contingency             | -                            | 0.2            |
| <b>Total</b>            | <b>\$13.0</b>                | <b>\$7.9</b>   |

Source: Vendor Recommendation Report and Draft Project Charter

The Project Charter, which represented the formal statement of work for the Financial Management System, outlined the following primary business goals:

- To replace Government's existing financial systems with fully supported systems which are Year 2000 compliant;
- to revise the work processes as required to increase efficiency when appropriate;

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| Oracle and Other        | 2.0                          | 1.4            |
| Government Resources    | -                            | 0.7            |
| Travel                  | 1.0                          | 0.6            |
| Sub-total               | 10.4                         | 5.0            |
| Hardware and Peripheral | 1.4                          | 1.5            |
| Software                | 0.8                          | 0.9            |
| Training                | 0.4                          | 0.3            |
| Contingency             | -                            | 0.2            |
| <b>Total</b>            | <b>\$13.0</b>                | <b>\$7.9</b>   |

Source: Vendor Recommendation Report and Draft Project Charter

The Project Charter, which represented the formal statement of work for the Financial Management System, outlined the following primary business goals:

- To replace Government's existing financial systems with fully supported systems which are Year 2000 compliant;
- to revise the work processes as required to increase efficiency when appropriate;

### **3.8 A Review of the Financial Management System**

- to enhance management information and tools to access it; and
- to enable integration of Government's Financial Management systems.

#### **Scope and Objectives**

We completed our review of the Financial Management System project in October 1999. The objectives of the review were to:

- review the process and methodology used in system implementation;
- determine the costs and time frame of acquiring and implementing the new system;
- determine whether the stated project objectives were achieved; and
- conduct a review of the controls over the system which ensure that Government's financial transactions are authorized, accurate and complete.

#### **Conclusions**

In November 1998, Government completed the replacement of many of its key financial systems with a new integrated Financial Management System. The acquisition and implementation of the Financial Management System was one of the most significant information technology projects undertaken by Government, involving over 15 departments and 500 users at 31 different locations. The system was scheduled to be implemented by 5 October 1998 with an approved budget of \$7.9 million. Our review of the acquisition and implementation of this system indicated the following:

- In selecting a financial system, a Request for Proposals was not issued due to a number of considerations including what Government considered to be imposed time constraints in implementing a system that would be Year 2000 compliant. A Request for Information was sent to two vendors and responses from these vendors were evaluated jointly by Government and xwave solutions and in February 1997, Oracle was selected as the successful vendor.

### 3.8 A Review of the Financial Management System

This process is in accordance with the Service Level Agreement between Government and xwave solutions. This Agreement contains provisions which exempts Government from the *Public Tender Act* for such goods and services acquired from xwave solutions.

- An appropriate methodology, which details the various phases for a successful system implementation, was in place for the Financial Management System. The key stakeholders and decision makers met weekly to actively manage this project providing direct leadership to the project resources. We did note, however, that a project charter, which defines the management and work requirements for system implementation and is the main reference for resources working on the project, was not prepared until December 1997, some six months after Treasury Board approved the project and approximately \$1.9 million had been spent on the project. Other observations with respect to implementation methodology include a lack of operational support during initial system implementation and a lack of training for secondary users of the system as well as provision for continued training.
- The acquisition and implementation of the Financial Management System cost \$7.8 million up to the end of November 1998 when the core applications were implemented in all the departments. The budget for the Financial Management System was \$7.9 million.
- The target for system implementation was established for 5 October 1998. The project included the implementation of five core modules including budgeting, purchasing, accounts payable, accounts receivable and general ledger. The accounts receivable module consisted of a cash receipts function and an accounts receivable function. While the cash receipts function of the accounts receivable module was planned for implementation at the Central Cashier's Office by 5 October 1998, implementation of the accounts receivable function was limited to the Department of Works, Services and Transportation. Our review indicated that, by 17 November 1998, all core applications were fully operational with the exception of the accounts receivable function at the Department of Works, Services and Transportation. The accounts receivable function was implemented in 12 of the 15 departments between May and October of 1999. Continued implementation of the accounts receivable function is scheduled for 1999-2000.
- Project objectives of enabling integration of Government's financial management systems and replacing existing financial



### 3.8 A Review of the Financial Management System

systems with fully supported systems which have been assessed as Year 2000 compliant have been achieved with respect to the Financial Management System. Although not part of the scope of the Financial Management System project, other financial systems, such as payroll, operate independently of and are not integrated with this Financial Management System. In addition, some of these other financial systems are still not Year 2000 compliant.

Although management's access to certain information, such as available funds, has improved with the new system, departmental officials indicate that reports from the new system do not provide any additional information than was available from the previous system and financial reports are still not received on a timely basis. In addition, departments indicate that these reports are more cumbersome to review and understand due to the presentation of the information.

- Based on our review of the system, there are controls in place to ensure the authorization, accuracy and completeness of government's financial transactions. As with all systems, the successful operation of these controls depend on actions and procedures carried out by departmental personnel.

There were some control weaknesses noted which included the system not prompting users to change their password on a regular basis and the system not providing a cross-reference between responsibility centre and activity which can result in expenditures being distributed to the incorrect accounts. In addition, departments experienced problems with the system during fiscal year end when canceling a purchase order for the previous fiscal year or incorrectly processing previous year transactions in the new year and having to reverse these transactions. Instead of clearing the related encumbrance, the amount of this canceled encumbrance was added to the new fiscal year available fund balance thus providing an available fund balance in excess of that approved. As a result, certain departments exceeded the approved budget for certain activities and had to transfer available funds from other activities to cover the deficiency. We note that these weaknesses have recently either been addressed or are being addressed by Treasury Board Secretariat.

Treasury Board officials indicated that the risk of prolonged system outage has been eliminated by measures such as having a server at two different sites which run simultaneously, regular back-ups and provision for essential printers. However, Treasury Board Secretariat has not yet developed a disaster recovery plan to



### 3.8 A Review of the Financial Management System

deal with other aspects of a disaster such as the establishment of a disaster recovery team with assigned responsibilities, loss of work space and loss of computer peripheral equipment.

#### **Findings and Recommendation**

#### **Methodology for System Implementation**

An appropriate methodology must be in place in order to effectively implement an information technology project. Such a methodology would include obtaining adequate user input, clearly defining project requirements, mapping these requirements to the core applications being implemented and providing solutions where gaps exist. It would also include building and testing the software, testing the applications, preparing training and reference materials, establishing various levels of support, training users of the system, connecting users to the system, simulating production runs and converting data to the new system.

Our general overview of this area indicated that overall, an appropriate methodology was in place for the implementation of the Financial Management System. However, we did note the following observations:

- The Service Level Agreement between Government and NIS requires that a project charter document be in place for any large information technology projects. The purpose of this charter is to define the management and work requirements to undertake system implementation. The charter is the main mechanism for communication and agreement on various aspects of this project between Government and NIS and the main reference for resources working on the project. A draft project charter was not prepared until December 1997, some six months after Treasury Board approved the project and \$1.9 million in project expenditures had been incurred. The charter was not updated at the various main stages of the project nor was the project charter ever signed off to indicate appropriate approval.
- Upon completion of the various phases of the project, a phase end report was to be signed as reviewed and approved by the Project Management team and the designated Module Manager. This approval indicated that all requirements as stated in the Request for Information document had been satisfactorily addressed. In addition to the phase end reports being approved, the Comptroller General of Treasury Board Secretariat was to sign a stakeholder acceptance for each completed Module. Our review indicated that all phase end reports and Stakeholder Acceptance of the Modules were signed off for approval with the exception of the Budget System Phase End Report and the Technical Architecture Phase End Report. As a result, there is no documented evidence that

### 3.8 A Review of the Financial Management System

these phases were approved by the Project Management Team as having been satisfactorily completed as outlined in the Request for Information.

- Although a "help desk" was established to support departments during initial system implementation, department officials indicated that they generally felt that the original level of support was inadequate and the time frame for resolution of help requests was often quite excessive. During the period of 18 November 1998 to 14 May 1999 there were 1,730 help desk requests received from departments.
- Discussions with a number of officials from various departments indicated that although the primary or "power users" of the system appeared to generally receive adequate training, secondary users, who usually represent the approver of transactions, did not receive adequate training. Some departments also felt that continued training was required but not provided.
- With respect to connectivity to the system, certain departments reported initial difficulties accessing the system (Department of Justice with respect to Registrar of the Supreme Court, Royal Newfoundland Constabulary and H.M. Penitentiary) and many experienced difficulties printing information from the system. These issues have since been resolved although some departments are still experiencing difficulties with printing.

In reviewing the process for system selection, we noted that a Request for Proposals was not issued due to what Government considered to be imposed time constraints in implementing a system that would be Year 2000 compliant. A Request for Information was sent to two vendors and responses from these vendors were evaluated jointly by Government and NewTel Information Solutions Limited and in February 1997, Oracle was selected as the successful vendor. This process is in accordance with the Service Level Agreement between Government and xwave solutions (formally NewTel Information Solutions Limited). This Agreement contains provisions which exempts Government from the *Public Tender Act* for such goods and services acquired from xwave solutions.

#### Project Costs

To monitor project costs, the Project Management Team prepared a monthly summary of cumulative expenditures. As outlined in Figure 2, the cost of acquiring and implementing the Financial Management System project over the two year period was reported at \$7.5 million (Budget - \$7.9 million).



### 3.8 A Review of the Financial Management System

Figure 2

#### Financial Management System (\$ Millions)

| Expenditure Type         | Project Budget | Actual Costs |              | Total Costs  | Variance - Actual to Budget |
|--------------------------|----------------|--------------|--------------|--------------|-----------------------------|
|                          |                | 1997/1998    | 1998/1999    |              |                             |
| Professional Services    |                |              |              |              |                             |
| NIS                      | 2.3            | 1.2          | 1.3          | 2.5          | 0.2                         |
| Oracle and Other         | 1.4            | 0.7          | 0.7          | 1.4          | -                           |
| Government Resources     | 0.7            | -            | 0.4          | 0.4          | (0.3)                       |
| Travel                   | 0.6            | 0.2          | 0.3          | 0.5          | (0.1)                       |
| Sub-total                | 5.0            | 2.1          | 2.7          | 4.8          | (0.2)                       |
| Hardware and Peripherals | 1.5            | 1.3          | 0.2          | 1.5          | -                           |
| Software                 | 0.9            | 1.0          | -            | 1.0          | 0.1                         |
| Training                 | 0.3            | 0.2          | -            | 0.2          | (0.1)                       |
| Contingency              | 0.2            | -            | -            | -            | (0.2)                       |
| <b>Total</b>             | <b>\$7.9</b>   | <b>\$4.6</b> | <b>\$2.9</b> | <b>\$7.5</b> | <b>(\$0.4)</b>              |

Source: Draft Project Charter and Project Management Team Financial Summary

Our review of these costs indicated the following:

- The \$7.5 million included costs incurred up to the end of November 1998 when the core applications were implemented in all the departments. After this date, costs relating to the operations of the Financial Management System were no longer tracked by the Project Management Team but continued to be accumulated by the Information Technology Division in Treasury Board Secretariat as part of Governments overall IT expenditures. Although Treasury Board Secretariat could not readily provide us with costs incurred after the end of November, a review of the larger NIS billings to Government between the period 1 December 1998 and 30 September 1999, indicate that an estimated additional \$1.1 million in expenditures were incurred under NIS's work order established for the implementation of the new financial system.

### 3.8 A Review of the Financial Management System

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| Expenditure Type         | Project Budget | Actual Costs |              | Total Costs  | Variance - Actual to Budget |
|--------------------------|----------------|--------------|--------------|--------------|-----------------------------|
|                          |                | 1997/1998    | 1998/1999    |              |                             |
| Professional Services    |                |              |              |              |                             |
| NIS                      | 2.3            | 1.2          | 1.3          | 2.5          | 0.2                         |
| Oracle and Other         | 1.4            | 0.7          | 0.7          | 1.4          | -                           |
| Government Resources     | 0.7            | -            | 0.4          | 0.4          | (0.3)                       |
| Travel                   | 0.6            | 0.2          | 0.3          | 0.5          | (0.1)                       |
| Sub-total                | 5.0            | 2.1          | 2.7          | 4.8          | (0.2)                       |
| Hardware and Peripherals | 1.5            | 1.3          | 0.2          | 1.5          | -                           |
| Software                 | 0.9            | 1.0          | -            | 1.0          | 0.1                         |
| Training                 | 0.3            | 0.2          | -            | 0.2          | (0.1)                       |
| Contingency              | 0.2            | -            | -            | -            | (0.2)                       |
| <b>Total</b>             | <b>\$7.9</b>   | <b>\$4.6</b> | <b>\$2.9</b> | <b>\$7.5</b> | <b>(\$0.4)</b>              |

Source: Draft Project Charter and Project Management Team Financial Summary

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### 3.8 A Review of the Financial Management System

We reviewed supporting documentation for this \$1.1 million; however, we could not determine whether this work related to further refinement of the system or to regular system operations support. Treasury Board Secretariat officials indicate that this \$1.1 million related to systems operations support and was not part of the system acquisition and implementation.

- Not all costs associated with personnel from across government who participated in implementation of the five core applications were included in the cost of \$7.5 million. These additional costs are estimated at \$380,000; however, the personnel representing \$130,000 of this \$380,000 were not included in the original project budget of \$7.9 million.
- Other expenditures were incurred by departments in relation to the Financial Management System, including certain infrastructure upgrades and personnel overtime associated with processing backlog of invoices due to the increase in time required for the system to process data input. Although most departments could not readily indicate the total of these expenditures, the departments did not estimate the expenditure to be of a significant amount. Departments also indicated that similar expenditures were incurred for the maintenance and operational support for the previous financial systems. Officials from one of the larger departments, however, did indicate that due to the increased time required to input data for purchasing, the Department had to hire an additional 3 full-time staff at an estimated annual cost of \$90,000. In addition to this \$90,000, the department incurred an estimated \$100,000 in overtime to process invoice payments. This was due to the increase in time required for the system to process data input.
- The approved estimates for 1999-2000 include \$6.9 million for the co-ordination of information technology matters within Government. Of this \$6.9 million, \$1.8 million has been allocated for any refinement to and maintenance and operational support for the Financial Management System. Treasury Board Secretariat officials could not provide any additional cost estimates on specific initiatives for the Financial Management System. Maintenance and operational support for the previous financial system has been estimated by Government to cost \$1.4 million.



### **3.8 A Review of the Financial Management System**

#### **Project Schedule**

The target for system implementation was established for 5 October 1998. The project included the implementation of the following five core applications:

1. Invoice Processing/Accounts Payable/Payments and Bank Reconciliation
2. Accounts Receivable/Cash Receipting
3. General Ledger and Project Costing
4. Budgetary Control and Budget Preparation and Monitoring
5. Purchasing

The accounts receivable module consisted of a cash receipts function and an accounts receivable function. While the cash receipts function of the accounts receivable module was planned for implementation at the Central Cashier's Office by 5 October 1998, implementation of the accounts receivable function was limited to the Department of Works, Services and Transportation.

Our review indicated that, by 17 November 1998, all core applications were fully operational with the exception of the accounts receivable function at the Department of Works, Services and Transportation. The accounts receivable function was implemented in 12 of the 15 departments between May and October of 1999. Continued implementation of the accounts receivable function is scheduled for 1999-2000.

Although the remaining core applications were operational by November 1998, there were a number of issues within each application that were deferred. These items had been assessed by the Project Management Team as not being mandatory for system start-up. Such issues include determining how to modify financial reports to meet user requirements, how to provide certain statistical information to other agencies like Statistics Canada as had been provided in the past, and what procedures to conduct in the preparation of the Consolidated Revenue Fund financial statements at fiscal year end. Our review of these items also indicated that they were not of a significant nature to impede the functionality of system operations. Treasury Board officials indicate that these deferred issues have become part of Government's Information Technology Division's and as well the Office of the Comptroller General's work plan and will be addressed accordingly.



### 3.8 A Review of the Financial Management System

#### Project Objectives

To determine whether the stated project objectives, as outlined in the Project Charter, were achieved, we conducted interviews with various departmental officials to assess these objectives against the actual project outcomes. Our review of this area indicated the following with respect to each objective:

1. *To replace Government's existing financial systems with fully supported systems which are Year 2000 compliant.*

As of October 1999, with the exception of the Accounts Receivable module, all core applications have been implemented and tested by Government, NIS and Oracle to be Year 2000 compliant. We do note, however, that certain systems outside of the scope of the new Financial Management System, continue to be refined or implemented for the purposes of being Year 2000 compliant. Such systems include the Taxation Administration Management System which is not anticipated to be Year 2000 compliant until the end of October 1999.

2. *To revise the work processes as required to increase efficiency when appropriate.*

The scope of the project was restricted to the replacement of current system functionality only. A policy decision was taken that there would be no customization of the basic suite of products and business processes would be changed to accommodate this policy. Thus this policy would not necessarily provide for more efficient business processes.

Discussions with departments indicate that invoice processing has become less efficient on the new Financial Management System due to the level of detail and screens that are required to be completed during data input. Departments also indicate this additional effort does not result in enhanced financial information. However, as a result of the above policy, it is difficult to determine whether invoice processing could or should have improved.

3. *To enhance management information and tools to access it.*

As the core applications now integrate with one another, management's access to information is enhanced. We do note, however, that while systems were under development departments were not able to obtain reports on outstanding encumbrances from the period of early December 1998 to late February 1999. Thus,

### 3.8 A Review of the Financial Management System

for this period, it was difficult for departments to know whether they had sufficient funds to pay for planned expenditures or expenditures incurred. This issue has since been resolved and departments have access to available funds at any point in time which is an enhancement of the previous system.

With respect to the objective of enhancing management information, departmental officials indicate that reports from the new system do not provide any additional information than was available from the previous system and information contained in the reports is still not received on a timely basis. Monthly reports on revenue and expenditure transactions are normally not received until two to three weeks after the end of the month to which the transactions relate. This reduces the usefulness of the information as it becomes more of a historical record rather than for use in facilitating management planning and decision making. Departments also indicated that reports from the new system are more cumbersome to review and understand due to the presentation of the information in the report.

#### 4. *To enable integration of Government's Financial Management systems.*

The five core applications of the Financial Management System which includes budgeting, purchasing, accounts payable, accounts receivable and general ledger operate as a fully integrated system. In addition to these five core applications, other financial systems are maintained independent of the Financial Management System including the Human Resource Management Information System (payroll and position administration), payments to one-time vendors, Motor Registration Division System, Taxation Information Management System and the Inventory Management System.

Information from these other systems are processed into the Financial Management System through the use of computer interfaces. Although not part of the scope of the Financial Management System Project, Treasury Board Secretariat is considering future integration of the Financial Management System with payroll, capital assets, management reporting, inventory control and cash management. If this future integration was achieved, Government systems would be fully integrated which may facilitate access to and the preparation of more timely and complete financial information.

### **3.8 A Review of the Financial Management System**

#### **System Controls**

To ensure that Government's financial transactions are authorized, accurate and complete, we conducted a review of the application and environmental controls over the new Financial Management System. In conducting our review, we relied on information obtained through interviews with, and documentation obtained from, departmental staff. We also tested various system controls by reviewing a sample of invoices being processed.

Based on our review of the system, there are controls in place to ensure the authorization, accuracy and completeness of government's financial transactions. As with all systems, the successful operation of these controls depend on actions and procedures carried out by departmental personnel. We also note that in addition to system controls, other controls exist outside the system including such controls as the segregation of incompatible duties (purchasing, receiving and payables), manual approval of invoices for receipt of goods and accuracy of invoice, and an internal audit function which reviews selected transactions for accuracy and appropriateness. This report, however, focuses on the system controls which include, but are not limited to the following:

- Access to the system is centrally controlled by Treasury Board Secretariat through the use of an assigned user ID and password. Access is further controlled through the assignment of a level of responsibility to users which limits the functions users have access to. An additional security feature restricts the values a user can use during data entry.
- Account and vendor maintenance is performed centrally by Treasury Board Secretariat.
- Changes to systems and application programs are centrally controlled and have to be appropriately approved.
- System edits require that funds encumbered have to be entered and approved by two different individuals and funds must be available for this expenditure object before the system will process the encumbrance request.
- The system monitors data input for invoices relative to pre-determined control totals (number of invoices and total dollar value) and data will not be processed further unless the input totals match the pre-determined control totals.

### 3.8 A Review of the Financial Management System

- Numerous system edits exist including that the same invoice number cannot be entered twice for any one vendor, the accounting period open is valid, the account combination and supplier numbers are valid, the entry must be balanced and invoice amount must equal purchase order amount.
- System edits require that invoices have to be entered and approved by two different individuals and the approver cannot alter any invoice information that was entered.
- Journal entries can only be performed by a specific individual in each department and the system will not allow the same individual to enter and approve the same journal entry. The entry must be balanced before the system can process the entry.
- Pre-determined control totals in the Accounts Payable module are balanced to the General Ledger totals.
- Data rejected from the processing cycle are entered into an error log for follow up.

We did note, however, the following observations with respect to system weaknesses:

- Although the system has been operational since the fall of 1998, users were not prompted by the system to change their password until August 1999. Departmental officials informed us that the system will now prompt users to change their password every 90 days. Changing passwords on a regular basis reduces the risk of an unauthorized individual gaining access to an authorized users password.

In addition, a listing of authorized system users and the system functions to which they have access was not circulated to departments for review until July 1999. Treasury Board Secretariat officials indicated that a listing will now be circulated to departments approximately every six months. A review of these listings by departments should detect unauthorized system access rights and also ensure that all persons on the listings are current employees of the department.

### 3.8 A Review of the Financial Management System

- The system does not provide a cross-reference between responsibility centre and activity as it did in the previous system. As a result, expenditures can be processed to the wrong activity and the system will not highlight these as invalid. This also reduces the usefulness of financial information as these errors may not be detected by those who review the reports.
- Departments experienced problems with the system during fiscal year end. This problem related to canceling a purchase order for the previous fiscal year or incorrectly processing previous year transactions in the new year and having to reverse these transactions. The system, instead of clearing the related encumbrance, added the amount of this canceled encumbrance to the new fiscal year available fund balance thus providing an available fund balance in excess of that approved. As a result, certain departments exceeded the approved budget for certain activities and had to transfer available funds from other activities to cover the deficiency. Treasury Board Secretariat officials indicate that Oracle is still trying to resolve this issue. In the interim, Treasury Board Secretariat officials run a nightly report for each department to detect this problem and correct the fund balance before processing occurs the next day.

We also reviewed the controls designed to reduce the chance of a disaster or to enhance the ability to recover from one within an acceptable period of time. To minimize the disruption to operations that may be caused by an unforeseen event such as a fire, it is necessary for Government to have a detailed and proven disaster recovery plan. Treasury Board officials indicated that the risk of prolonged system outage has been eliminated by measures such as having a server at two different sites which run simultaneously, regular back-ups and provision for essential printers. However, Treasury Board Secretariat has not yet developed a disaster recovery plan to deal with other aspects of a disaster such as the establishment of a disaster recovery team with assigned responsibilities, loss of work space and loss of computer peripheral equipment.

#### **Recommendation**

*Treasury Board Secretariat should consider the issues raised in this report and take corrective action where necessary.*

### 3.8 A Review of the Financial Management System

#### **Treasury Board Secretariat's Response**

*Although I totally agree with your observations and findings, I must state that I was very pleased with the implementation by government staff and contracted consultants of this major project on time and under budget. I feel that the conduct of the project reflects well on the ability and initiative of government's staff.*

*With respect to the recommendations contained throughout your report, I agree with your observation that many either have already been implemented or are in the process of being implemented. The remaining significant recommendations will be acted upon in the near future.*



### 3.9 Repayment of Severance and Redundancy Pay

#### Introduction

Government has undertaken a number of initiatives in recent years to decrease the size of the public service. As part of Government's effort to assist employees displaced as a result of these initiatives, in December 1990 Government revised its Re-employment Priority Policy which addresses many aspects of the needs of displaced workers. For example, Government provides counselling services, alternate employment services, relocation benefits, redundancy pay, and severance pay.

During 1996-97, 1997-98 and 1998-99, Government and its Crown agencies paid a total of \$67.5 million in ex-gratia and other payments. A significant portion of the \$67.5 million was redundancy and severance paid to displaced employees of Government departments, school boards, health care boards and other Crown agencies. Figure 1 provides a summary of ex-gratia and other payments made over the past three fiscal years.

**Figure 1**

#### Ex-gratia and Other Payments Years ended 31 March \$ Millions

| Entity                                 | 1996-97 | 1997-98 | 1998-99 | Total  |
|----------------------------------------|---------|---------|---------|--------|
| Government Departments                 | \$21.8  | \$17.6  | \$2.3   | \$41.7 |
| Pooled Pension Fund                    | 5.9     | 5.5     | 5.1     | 16.5   |
| Health Care Boards                     | 1.5     | 0       | 0       | 1.5    |
| School Boards                          | .5      | .1      | 1.0     | 1.6    |
| Community Colleges                     | .8      | .9      | .7      | 2.4    |
| Newfoundland Farm Products Corporation | 0       | 3.8     | 0       | 3.8    |
| Total                                  | \$30.5  | \$27.9  | \$9.1   | \$67.5 |

Source: Government's Financial Statements and Accounting Records





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#### Introduction

Government has undertaken a number of initiatives in recent years to decrease the size of the public service. As part of Government's effort to assist employees displaced as a result of these initiatives, in December 1990 Government revised its Re-employment Priority Policy which addresses many aspects of the needs of displaced workers. For example, Government provides counselling services, alternate employment services, relocation benefits, redundancy pay, and severance pay.

During 1996-97, 1997-98 and 1998-99, Government and its Crown agencies paid a total of \$67.5 million in ex-gratia and other payments. A significant portion of the \$67.5 million was redundancy and severance paid to displaced employees of Government departments, school boards, health care boards and other Crown agencies. Figure 1 provides a summary of ex-gratia and other payments made over the past three fiscal years.

Figure 1

#### Ex-gratia and Other Payments Years ended 31 March \$ Millions

| Entity                                 | 1996-97 | 1997-98 | 1998-99 | Total  |
|----------------------------------------|---------|---------|---------|--------|
| Government Departments                 | \$21.8  | \$17.6  | \$2.3   | \$41.7 |
| Pooled Pension Fund                    | 5.9     | 5.5     | 5.1     | 16.5   |
| Health Care Boards                     | 1.5     | 0       | 0       | 1.5    |
| School Boards                          | .5      | .1      | 1.0     | 1.6    |
| Community Colleges                     | .8      | .9      | .7      | 2.4    |
| Newfoundland Farm Products Corporation | 0       | 3.8     | 0       | 3.8    |
| Total                                  | \$30.5  | \$27.9  | \$9.1   | \$67.5 |

Source: Government's Financial Statements and Accounting Records

### 3.9 Repayment of Severance and Redundancy Pay

#### Conclusions

Section 17 of the *Financial Administration Act* indicates that the Minister of Finance may, subject to the approval of the Lieutenant-Governor in Council and another Act, negotiate and accept a settlement of a debt. Treasury Board Secretariat did not have the approval of the Lieutenant-Governor in Council as required by the *Financial Administration Act* when it issued its Directive stating that employees who are required to repay redundancy and/or severance benefits have the option of making lump sum repayments or negotiating a repayment schedule acceptable to their department based on their ability to pay and the salary earned in their new position. As a result, Government is in contravention of the *Financial Administration Act*.

Government's policy is unclear as to who is responsible for ensuring amounts owing for severance and redundancy pay are actually collected by Government. Furthermore, Government has not carried out any reviews to ensure employees who received severance and/or redundancy payments, and who were subsequently rehired by Government departments, Crown corporations, and other Government agencies, repay amounts owing in accordance with Government policy.

Although Minute of Council 94-520 indicates that compensation practices of Government are applicable to Crown corporations and other Government agencies, Government's current policy is silent on the issue of rehiring in these entities. Government's current policy does not address the repaying of severance and redundancy pay if an employee of one Government entity obtains employment with another Government entity.

Of 24 employees selected for review to determine compliance with the *Financial Administration Act* and Government's Re-employment Priority Policy, we found the following instances of non-compliance:

- 6 employees were provided with the option of repaying their severance pay and/or redundancy pay over a period of time. Five of these 6 employees accepted this repayment option. These repayment options contravened the *Financial Administration Act*.
- 4 of these 6 employees had their repayment calculations, in part, based on their new lower salaries. The departments, therefore, reduced the amounts the employees were required to repay. In our opinion, under Section 17 of the *Financial Administration Act*, there is no authority for Departments to reduce amounts owing by rehired employees and therefore the reductions contravene the *Act*.

### 3.9 Repayment of Severance and Redundancy Pay

However, we do note that although in all 4 cases the departments are reducing the amounts owed by the employees based on the employees new lower salaries, the departments used the employees gross amount received and not the net as is allowed in accordance with the General Service Collective Agreement signed 21 April 1998. This resulted in 3 of the 4 employees actually paying more than they would have if the provision in the Collective Agreement was followed. However in the fourth case, because of errors in the calculation of the amounts due, the employee has paid less than the amount required to be repaid.

- 3 rehired employees did not repay their severance pay and/or redundancy pay in accordance with Government policy and Government did not pursue collection of amounts due.

We also found an instance where an employee's repayment amount was based on the individual's new higher salary and resulted in the employee paying back more redundancy pay than was originally received.

Although an employee commenced an employment contract with one department a week before their employment was terminated at another department, the individual was provided with severance pay and redundancy pay totalling \$53,037. I am concerned that Government would enter into an arrangement which provided severance pay and redundancy pay totalling \$53,037 to an employee while ensuring that the employee retained a position within Government with exactly the same salary and benefits. In addition, as a result of the overlap in the contract commencement date and the employee's redundancy date, the employee was paid \$1,298 for six days as a salaried employee and \$1,298 for the same six days under their employment contract. The employee did not repay any of the \$53,037 relating to severance pay and redundancy pay or any of the duplicate salary payment of \$1,298.

In 1998, a former employee of a health care corporation terminated employment and received a payment of \$30,000. This did not represent severance as the employee accepted employment with another public service entity and, in accordance with Government policy, carried the years of service forward to that entity. There was no authority for the corporation to pay this \$30,000.

### 3.9 Repayment of Severance and Redundancy Pay

#### Findings and Recommendations

##### 1. Review of policy

As outlined in Government's Personnel Administration Procedures Manual, employees who voluntarily terminate or involuntarily terminate (through redundancy) their employment are eligible for severance pay at the rate of one week of pay for each year of past employment with Government provided the employee has a minimum of nine years of continuous service. The maximum payable for severance pay is twenty weeks salary.

In addition to severance pay, employees whose employment is terminated by Government, are eligible for redundancy pay which is effectively pay in lieu of notice. The amount paid to an employee depends upon their age and length of service. Government's Personnel Administration Procedures includes a grid which outlines the number of weeks of pay to which employees are entitled based on their age and length of service.

If an employee has received severance and/or redundancy pay and is subsequently rehired, Government's Personnel Administration Procedures policy states that the employee shall be required to pay back part of any severance pay and/or redundancy pay they received. The amount that the employee has to repay is based on the length of time the employee has been out of the public service.

Figure 2 outlines Treasury Board's interpretation of the repayment provisions of the re-employment and priority policy contained in Government's Personnel Administration Procedures.

**Figure 2**

#### Policy on Repayment of Severance and Redundancy Pay

| Re-employment                                                                            | Severance             | Redundancy                                                                           |
|------------------------------------------------------------------------------------------|-----------------------|--------------------------------------------------------------------------------------|
| 1. re-employed into a permanent position during the redundancy notice period             | Repay All             | Repay portion which overlaps with period of re-employment.                           |
| 2. re-employed into a temporary or seasonal position during the redundancy notice period | Not required to repay | Repay the portion which overlaps with period of temporary or seasonal re-employment. |
| 3. re-employed in permanent, temporary or seasonal position after redundancy period      | Not required to repay | Not required to repay.                                                               |

Source: Treasury Board Directive, 8 April 1997

### 3.9 Repayment of Severance and Redundancy Pay

Treasury Board's interpretation of the repayment provisions of the re-employment and priority policy contained in Government's Personnel Administration Procedures Manual provides guidance on redundancy pay and severance pay including the repayment of these benefits. Specifically, employees who are required to repay redundancy and/or severance benefits have the option of making lump sum repayments or negotiating a repayment schedule acceptable to their department based on their ability to pay and the salary earned in their new position.

In addition, Article 37.01 of the General Service Collective Agreement signed 21 April 1998 provides that the amount of severance and/or redundancy pay to be repaid shall be based on the net (our emphasis) amount received by the employee and/or the amount paid to a financial institution on behalf of the employee.

Our review of Government's policy with respect to the recovery of severance and/or redundancy entitlements from employees who were rehired by Government after termination of employment indicated the following:

- A Treasury Board Directive dated 8 April 1997, states that employees who are required to repay redundancy and/or severance entitlements have the option of making lump sum repayments, or negotiating a repayment schedule acceptable to management based on their ability to pay and the salary earned in their current position. However, Section 17 of the *Financial Administration Act* indicates that the Minister of Finance may, subject to the approval of the Lieutenant-Governor in Council and another Act, negotiate and accept a settlement of a debt. Treasury Board Secretariat did not have the approval of the Lieutenant-Governor in Council as required by the *Financial Administration Act* relating to the policy of permitting individuals to negotiate a repayment schedule and therefore, is in contravention of the *Act*.
- Government's policy is unclear as to who is responsible for ensuring amounts owing for severance and/or redundancy pay are actually collected by Government. While some Government officials indicated that the responsibility of identifying amounts that have to be repaid rests with the hiring department, Crown corporation or other government agency, other officials indicated that they did not know.



### **3.9 Repayment of Severance and Redundancy Pay**

- Minute of Council 94-520 indicates that compensation practices of Government are applicable to Crown corporations and other Government agencies. As a result, employees who received severance and/or redundancy pay upon termination of employment with Crown corporations and other Government agencies are required to repay the amounts in accordance with Government policy. Government does not know the extent to which Crown corporations and other Crown agencies are complying with the policy.
- There is no review by Government to ensure compliance with its repayment of severance and redundancy pay policy by departments, Crown corporations, and other Government agencies.
- Article 37.01 of the General Service Collective Agreement is not equitable. For example, two individuals having identical positions and identical length of service with Government will experience different financial results depending on whether they roll their severance and/or redundancy pay into an RRSP or opt to receive payment. The individual choosing to roll their severance and/or redundancy pay into an RRSP will be required to repay the gross amount. The individual opting to receive payment, however, would only be required to repay the net amount under Article 37.01 of the Collective Agreement.

#### **2. Review of compliance with policy**

To determine whether Government was complying with its policy regarding the recovery of severance and/or redundancy pay, we selected a sample of former employees of Government departments who were subsequently re-hired.

To select the sample, we compared Government's listing of former employees who received severance pay and/or redundancy pay during 1996, 1997 and 1998 to Government's 31 March 1999 payroll to identify former employees who were subsequently re-employed. Of the 1,142 former employees on Government's listing who received severance and/or redundancy pay, 113 employees were on the payroll as at 31 March 1999.

We reviewed 11 of these 113 employees to determine whether they should have repaid their severance and/or redundancy pay, and whether in fact repayments had actually been made. In addition, we selected 13 other employees identified during other audits to determine whether any severance and/or redundancy pay received should have been repaid.



### 3.9 Repayment of Severance and Redundancy Pay

Of the 24 employees selected for review, we found instances of non-compliance with the *Financial Administration Act* and Government's Re-employment Priority Policy relating to 9 employees as follows:

#### (a) Non-compliance with the Financial Administration Act

Section 17 of the *Financial Administration Act* indicates that the Minister of Finance may, subject to the approval of the Lieutenant-Governor in Council and another Act, negotiate and accept a settlement of a debt. Treasury Board Secretariat did not have the approval of the Lieutenant-Governor in Council as required by the *Financial Administration Act* to permit individuals to negotiate a repayment schedule.

We found that 6 employees were provided with the option of repaying their severance pay and/or redundancy pay over a period of time. Five of these 6 employees accepted this repayment option. These repayment options contravened the *Financial Administration Act*.

We also found that 4 of these 6 employees had their repayment calculations, in part, based on their new lower salaries rather than the salaries on which their severance pay and/or redundancy pay was based. The departments, therefore, reduced the amounts the employees were required to repay. In our opinion, under Section 17 of the *Financial Administration Act*, there is no authority for Departments to reduce amounts owing by rehired employees and therefore the reductions contravene the *Act*.

In all 4 cases the departments are reducing the amounts owed by the employees based on the employees new lower salaries. However, employees are repaying the gross amount received and not the net amount received as is allowed in accordance with the General Service Collective Agreement signed 21 April 1998. This resulted in 3 of the 4 employees actually paying more than they would have if the provision in the Collective Agreement was followed. However in the fourth case, because of errors in the calculation of the amounts due, the employee will not pay the amount they were required to repay.

#### (b) Non-compliance with Government's Re-employment Priority Policy

Government policy requires that employees who receive severance and/or redundancy pay and who are subsequently rehired shall be required to pay back part of any severance pay

### 3.9 Repayment of Severance and Redundancy Pay

and/or redundancy pay they received. The amount that the employee has to repay shall be based on the length of time the employee has been out of the public service.

We found 3 rehired employees who did not repay their severance pay and/or redundancy pay in accordance with Government policy and Government did not pursue collection of amounts due.

We also found an instance where an employee's repayment amount was based on the individual's new higher salary and resulted in the employee repaying more redundancy pay than was originally received.

#### Other Comments

- One employee received \$53,037 comprised of \$20,565 in severance pay and \$32,472 in redundancy pay. The employee's position was declared redundant on 20 May 1997; however, on 13 May 1997 one week prior to their termination, Government and the employee entered into a contract whereby the employee would continue to be employed with Government. I am concerned that Government would enter into an arrangement which provided severance pay and redundancy pay totalling \$53,037 to an employee while ensuring that the employee retained a position within Government with exactly the same salary and benefits. In addition, as a result of the overlap in the contract commencement date and the employee's redundancy date, the employee was paid \$1,298 for six days as a salaried employee and \$1,298 for the same six days under their employment contract.

The employee did not repay any of the severance pay of \$20,565 or any of the redundancy pay of \$32,472 since contractual positions are not covered by the repayment terms of the policy. In addition, the employee did not repay any of the duplicate salary payment of \$1,298.

- In 1998, a former employee of a health care corporation terminated employment and received a payment of \$30,000. This did not represent severance as the employee accepted employment with another public service entity and, in accordance with Government policy, carried the years of service forward to that entity. There was no authority for the corporation to pay this \$30,000.

### 3.9 Repayment of Severance and Redundancy Pay

#### **Recommendations**

*Government should comply with the Financial Administration Act.*

*Government should identify all employees who received severance pay and/or redundancy pay and who were subsequently rehired and ensure that all amounts required to be repaid by these individuals are repaid.*

#### **Treasury Board Secretariat's Response**

*Treasury Board does not agree with the Auditor General's interpretation of Section 17 of the Financial Administration Act (FAA). The repayment of monies as a result of the rehire of a redundant employee is not captured under Section 17 because there was no settlement of the owed amount. In other words, Government did not negotiate to take less than the amount it was entitled to recover. All that occurred was the determination of the amount of the debt owed and the repayment of monies over a period of time as opposed to by lump sum payment.*

*From a practical perspective, the employing Department or Agency is the most appropriate vehicle to recover monies from the staff they hire. Treasury Board will direct Departments and Agencies to ensure this is done.*

*Compensation policies in Crown Corporations may not be identical to Government's because of legislation. Some Crown Corporations have been vested with significant latitude in their compensation and related policies by the legislature. For this reason MC 94-520 may not be universally applied. It is noted that legislation normally overrides policies established by MC.*

*There is no universal review by Government to ensure compliance with the repayment options. Again it is felt the employing Departments or Agencies are the most appropriate vehicle to achieve the repayment of monies. Treasury Board will direct Departments and Agencies to review their payroll files to determine if any cases exist where some corrective action needs to be taken.*

*The terms and conditions of the Collective Agreement, including any issues of what is equitable, have been negotiated and agreed to by the parties to the Agreement ie. the union and the Employer. We intend to review the manner in which the agreement is being interpreted, in light of the Auditor General's comments.*

*Treasury Board Directive 97-03 states, in part, that:*

- 1. An employee is obligated to repay severance and redundancy entitlements under the following conditions:*

### 3.9 Repayment of Severance and Redundancy Pay

- (i) *if a person is reemployed into a permanent position during the redundancy notice period, he/she has to repay all his/her severance pay and the portion of redundancy pay which overlaps with his/her period of reemployment.*
  - (ii) *if a person is reemployed into a temporary or seasonal position during the redundancy notice period, he/she has to repay the portion of redundancy pay which overlaps with his/her period of temporary or seasonal reemployment. However, he/she is not required to repay severance pay.*
  - (iii) *if a person is permanently, temporarily or seasonally reemployed after his redundancy notice period expires, he/she is not required to repay either the severance or redundancy pay.*
2. *Employees who are required to repay redundancy and/or severance entitlements have the option of making lump sum repayments, or negotiating a repayment schedule acceptable to management based on their ability to pay and the salary earned in their current position. The Human Resources Division is responsible for negotiating the repayment schedule.*

*The Auditor General feels that this violates Section 17 of the Financial Administration Act. Her draft report indicates her view that repayment be based on the employee's net pay but repaid at the former rate of pay. As noted above, Treasury Board requested repayment of the gross amount but repaid at the rehired employee's current rate of pay.*

*The Auditor General has raised issues concerning the repayment of severance and/or redundancy payments by employees who were subsequently rehired that require further review. Treasury Board will review this issue further and report back.*

### 3.10 Strategic Enterprise Development Fund

#### Introduction

The Strategic Enterprise Development Fund is administered by the Department of Development and Rural Renewal. The Fund provides capital financing to assist the start up and growth of small and medium sized businesses which have activities consistent with strategic sectoral opportunities identified as zonal or provincial priorities and whose funding needs cannot be met through other sources. Capital financing may take the form of loan advances, equity advances, loan guarantees, company development grants or conditional forgivable loans.

The Province provided \$18,100,000 to the Fund in 1996-97, \$7,000,000 in 1997-98 and \$8,975,000 in 1998-99. These funds were then transferred to Enterprise Newfoundland and Labrador (ENL) to provide capital financing to various individuals and entities. ENL was established under the authority of the *Enterprise Newfoundland and Labrador Corporation Act*. Effective 14 March 1996, the functions and staff of ENL were transferred to the Department of Development and Rural Renewal; however, ENL, until it is wound up, is still being used to report the transactions and balances of the Fund. Figure 1 shows the disbursements of the funds for the years 1997-98 and 1998-99.

Figure 1

**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Fund Disbursements  
For the Year Ended 31 March  
(\$000's)**

| Region   | 1998   |         |         |         | 1999   |          |         |          |
|----------|--------|---------|---------|---------|--------|----------|---------|----------|
|          | Grants | Loans   | Equity  | Total   | Grants | Loans    | Equity  | Total    |
| Avalon   | \$149  | \$925   | \$1,112 | \$2,186 | \$183  | \$2,100  | \$1,543 | \$3,826  |
| Eastern  | 26     | 368     | -       | 394     | 59     | 1,015    | -       | 1,074    |
| Central  | 131    | 633     | -       | 764     | 204    | 1,467    | 109     | 1,780    |
| Western  | 53     | 1,225   | -       | 1,278   | 199    | 1,908    | 78      | 2,185    |
| Labrador | 10     | 967     | -       | 977     | 44     | 1,239    | -       | 1,283    |
| Special  | -      | 1,800   | -       | 1,800   | -      | 4,589    | -       | 4,589    |
| Total    | \$369  | \$5,918 | \$1,112 | \$7,399 | \$689  | \$12,318 | \$1,730 | \$14,737 |

Source: Analysis of Department's Loans Administrator System





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Enterprise Newfoundland and Labrador  
Fund Disbursements  
For the Year Ended 31 March  
(\$000's)**

| Region   | 1998   |         |         |         | 1999   |          |         |          |
|----------|--------|---------|---------|---------|--------|----------|---------|----------|
|          | Grants | Loans   | Equity  | Total   | Grants | Loans    | Equity  | Total    |
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| Special  | -      | 1,800   | -       | 1,800   | -      | 4,589    | -       | 4,589    |
| Total    | \$369  | \$5,918 | \$1,112 | \$7,399 | \$689  | \$12,318 | \$1,730 | \$14,737 |

Source: Analysis of Department's Loans Administrator System



### 3.10 Strategic Enterprise Development Fund

The level of risk associated with these loans is high considering that one of the criteria for a business to receive funding is there be a lack of other funding sources. Figure 2 illustrates that, as at 31 March 1999, 67% of ENL's loan portfolio and 100% of the equity portfolio is unlikely to be recovered. In summary, only 25% of ENL's total loan and equity portfolio of \$78.2 million is estimated to be collectible.

**Figure 2**

**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Loans and Equity Investments  
For the Year Ended 31 March  
(\$ Millions)**

| Financial Item         | 1997    |       | 1998    |       | 1999    |        |
|------------------------|---------|-------|---------|-------|---------|--------|
|                        | Amount  | %     | Amount  | %     | Amount  | %      |
| Loans Receivable       | \$ 63.3 | 100%  | \$ 60.1 | 100%  | \$ 59.5 | 100%   |
| Allowance for doubtful | (33.9)  | (54)% | (40.3)  | (67)% | (39.7)  | (67)%  |
| Net Loans Receivable   | 29.4    | 46%   | 19.8    | 33%   | 19.8    | 33%    |
| Equity Investments     | 17.4    | 100%  | 17.9    | 100%  | 18.7    | 100%   |
| Allowance for doubtful | (13.5)  | (78)% | (13.1)  | (73)% | (18.7)  | (100)% |
| Net Equity Investments | 3.9     | 22%   | 4.8     | 27%   | 0.0     | 0%     |
| Net Loans and Equity   | \$ 33.3 | 41%   | \$ 24.6 | 32%   | \$ 19.8 | 25%    |

Source: 1997, 1998 Audited Financial Statements and 1999 Unaudited Financial Statements

The loans receivable and equity investments as at 31 March 1999 was comprised of 1,134 loans totalling \$59.5 million and 132 equity accounts totalling \$18.7 million. A further analysis of the 1,134 loans outstanding totalling \$59.5 million as at 31 March 1999 (1998- \$60.1 million) shows that there has been some arrears on 950 loans, totalling \$50.2 million. These arrears comprise \$15.0 million of the \$50.2 million.

### 3.10 Strategic Enterprise Development Fund

An analysis of these accounts indicated that these 1,266 loans/investments were provided to 964 companies or individuals. A further review indicated that 16 companies (1.6%) accounted for \$22.7 million (29.0%) of the total \$78.2 million principal outstanding as at 31 March 1999 as disclosed in Figure 3. Fourteen of these 16 are doubtful of collection, one has been repaid from other funding and one principal balance of \$2.7 million is being repaid at \$5,000 per month.

Since 1996 the annual budget of ENL has declined and as a result the dollar value of loans and investments to any one project has also declined. From 1 April 1996 to 31 March 1999, ENL approved three individual investments in excess of \$500,000 each and 49 loans and investments between \$100,000 and \$500,000, averaging \$179,700. The remaining 416 investments, including 176 company development grants, were under \$100,000.

**Figure 3**

**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Stratification of Loan balances  
31 March 1999  
(\$ Millions)**

| Loan/Equity Stratification<br>Based Upon Principal<br>Balance Outstanding | # of<br>clients | %             | Total<br>Principal<br>Receivable | Total<br>Interest<br>Receivable* | Total<br>Receivable | %             |
|---------------------------------------------------------------------------|-----------------|---------------|----------------------------------|----------------------------------|---------------------|---------------|
| Over \$1,000,000                                                          | 10              | 1.0%          | 17.2                             | 2.2                              | 19.4                | 21.1%         |
| \$750,000 - \$999,999                                                     | 6               | 0.6%          | 5.5                              | .8                               | 6.3                 | 6.8%          |
| \$500,000 - \$749,999                                                     | 13              | 1.3%          | 7.6                              | 2.3                              | 9.9                 | 10.7%         |
| \$250,000 - \$499,999                                                     | 42              | 4.4%          | 15.5                             | 3.3                              | 18.8                | 20.4%         |
| \$100,000 - \$249,999                                                     | 72              | 7.5%          | 11.1                             | 2.0                              | 13.1                | 14.2%         |
| \$50,000 - \$99,000                                                       | 150             | 15.6%         | 10.5                             | 1.7                              | 12.2                | 13.3%         |
| \$0 - \$49,999                                                            | 671             | 69.6%         | 10.8                             | 1.6                              | 12.4                | 13.5%         |
| <b>Total</b>                                                              | <b>964</b>      | <b>100.0%</b> | <b>78.2</b>                      | <b>13.9</b>                      | <b>92.1</b>         | <b>100.0%</b> |

\* Includes interest on loans and equity investments as per Loans Administrator System.  
Source: Analysis of Loans Administrator System

### 3.10 Strategic Enterprise Development Fund

The level of risk associated with these loans is high considering that one of the criteria for a business to receive funding is there be a lack of other funding sources. Figure 2 illustrates that, as at 31 March 1999, 67% of ENL's loan portfolio and 100% of the equity portfolio is unlikely to be recovered. In summary, only 25% of ENL's total loan and equity portfolio of \$78.2 million is estimated to be collectible.

**Figure 2**

**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Loans and Equity Investments  
For the Year Ended 31 March  
(\$ Millions)**

| Financial Item         | 1997    |       | 1998    |       | 1999    |        |
|------------------------|---------|-------|---------|-------|---------|--------|
|                        | Amount  | %     | Amount  | %     | Amount  | %      |
| Loans Receivable       | \$ 63.3 | 100%  | \$ 60.1 | 100%  | \$ 59.5 | 100%   |
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| Allowance for doubtful | (13.5)  | (78)% | (13.1)  | (73)% | (18.7)  | (100)% |
| Net Equity Investments | 3.9     | 22%   | 4.8     | 27%   | 0.0     | 0%     |
| Net Loans and Equity   | \$ 33.3 | 41%   | \$ 24.6 | 32%   | \$ 19.8 | 25%    |

Source: 1997, 1998 Audited Financial Statements and 1999 Unaudited Financial Statements

The loans receivable and equity investments as at 31 March 1999 was comprised of 1,134 loans totalling \$59.5 million and 132 equity accounts totalling \$18.7 million. A further analysis of the 1,134 loans outstanding totalling \$59.5 million as at 31 March 1999 (1998- \$60.1 million) shows that there has been some arrears on 950 loans, totalling \$50.2 million. These arrears comprise \$15.0 million of the \$50.2 million.

### 3.10 Strategic Enterprise Development Fund

An analysis of these accounts indicated that these 1,266 loans/investments were provided to 964 companies or individuals. A further review indicated that 16 companies (1.6%) accounted for \$22.7 million (29.0%) of the total \$78.2 million principal outstanding as at 31 March 1999 as disclosed in Figure 3. Fourteen of these 16 are doubtful of collection, one has been repaid from other funding and one principal balance of \$2.7 million is being repaid at \$5,000 per month.

Since 1996 the annual budget of ENL has declined and as a result the dollar value of loans and investments to any one project has also declined. From 1 April 1996 to 31 March 1999, ENL approved three individual investments in excess of \$500,000 each and 49 loans and investments between \$100,000 and \$500,000, averaging \$179,700. The remaining 416 investments, including 176 company development grants, were under \$100,000.

**Figure 3**

**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Stratification of Loan balances  
31 March 1999  
(\$ Millions)**

| Loan/Equity Stratification<br>Based Upon Principal<br>Balance Outstanding | # of<br>clients | %             | Total<br>Principal<br>Receivable | Total<br>Interest<br>Receivable* | Total<br>Receivable | %             |
|---------------------------------------------------------------------------|-----------------|---------------|----------------------------------|----------------------------------|---------------------|---------------|
| Over \$1,000,000                                                          | 10              | 1.0%          | 17.2                             | 2.2                              | 19.4                | 21.1%         |
| \$750,000 - \$999,999                                                     | 6               | 0.6%          | 5.5                              | .8                               | 6.3                 | 6.8%          |
| \$500,000 - \$749,999                                                     | 13              | 1.3%          | 7.6                              | 2.3                              | 9.9                 | 10.7%         |
| \$250,000 - \$499,999                                                     | 42              | 4.4%          | 15.5                             | 3.3                              | 18.8                | 20.4%         |
| \$100,000 - \$249,999                                                     | 72              | 7.5%          | 11.1                             | 2.0                              | 13.1                | 14.2%         |
| \$50,000 - \$99,000                                                       | 150             | 15.6%         | 10.5                             | 1.7                              | 12.2                | 13.3%         |
| \$0 - \$49,999                                                            | 671             | 69.6%         | 10.8                             | 1.6                              | 12.4                | 13.5%         |
| <b>Total</b>                                                              | <b>964</b>      | <b>100.0%</b> | <b>78.2</b>                      | <b>13.9</b>                      | <b>92.1</b>         | <b>100.0%</b> |

\* Includes interest on loans and equity investments as per Loans Administrator System.  
Source: Analysis of Loans Administrator System

### 3.10 Strategic Enterprise Development Fund

#### Scope and Objectives

We completed our review of the Fund in May 1999. Our objectives were to assess whether:

- the assistance provided to business through ENL is appropriately approved and monitored in accordance with corporate policy; and
- appropriate performance reporting systems are in place and functioning to provide information to Department Executive and the House of Assembly. Our review of the performance reporting system will determine if strategic objectives have been defined and are being reported upon, whether performance indicators have been identified, targets have been established and actual performance against those targets have been captured and reported.

Our review focused upon the ENL loan and equity portfolios and did not encompass the former fisheries and farm portfolios as previously administered by the Fisheries Loan Board and the Farm Development Loan Board respectively.

Our review included the examination of a statistical sample of loan files to assess the application and approval processes, and the monitoring process. Files selected for assessing the application and approval processes were current files which were initiated from 1 April 1996 to 31 January 1999. Files selected for the assessment of the monitoring process were chosen from the 31 March 1998 accounts receivable trial balance. A select number of files with larger balances as at 31 March 1998 were selected for detailed review. Figure 4 outlines the extent of our sampling.

**Figure 4**

#### Department of Development and Rural Renewal Enterprise Newfoundland and Labrador Sample Size of File Review

| Sample Extension         | Application/<br>Approval Review | Monitoring<br>Review | Detailed<br>Review | Total<br>Sample | Total<br>Portfolio<br>31 March 1999 |
|--------------------------|---------------------------------|----------------------|--------------------|-----------------|-------------------------------------|
| Number of files reviewed | 36                              | 35                   | 15                 | 86              | 1,266                               |
| Dollar magnitude         | \$5,313,948                     | \$6,919,630          | \$22,118,653       | \$34,352,231    | \$78,182,796                        |

### 3.10 Strategic Enterprise Development Fund

#### Conclusions

Since March 1996, the Department of Development and Rural Renewal has been performing many of the functions previously performed by the Enterprise Newfoundland and Labrador Corporation. Although the Enterprise Newfoundland and Labrador Corporation continues to exist, its main purpose is to hold the small business loan portfolio and its Board of Directors and Corporate Transaction Committee approve certain loans and investments. Functions such as assessing and monitoring proposals and reporting on performance are now performed by the Department of Development and Rural Renewal. Our review indicated the following:

- Reporting on the performance of the small business loan program is inadequate. There are no reports on the actual number of jobs created or what economic benefit has resulted from the loan program. Each year approximately \$7.0 million is invested in this program without adequate structures in place to determine if the program is achieving its intended purpose and without any reports, other than audited financial statements, to the House of Assembly on what has been achieved. In June 1999 the Department prepared a report on approvals and employment by industry sector; however, this is an internal report and is not required on a regular basis. It was not provided to the House of Assembly.
- Assessment of loan proposals was not always adequate as significant pieces of information were not included in the assessment. Our review identified concerns with 7 of the 42 files reviewed regarding the adequacy of the assessment of the proposal.
- Loans were made to companies that had existing loans in arrears or when there were indications that management was not acting in good faith. Our review identified concerns with 7 of 42 files reviewed regarding the future viability of the proposal.
- Adequate security was not always obtained prior to the loan disbursement and funds were disbursed prior to conditions for the loan being met. Our review identified concerns with 4 of 42 files reviewed regarding the adequacy of security.
- Once the loans are issued there is inadequate follow up to ensure the conditions for the loan continue to be met. Required financial information is not always submitted to the regional offices and there are very few personal visits or contact with the loan clients. Without these visits the Department cannot ensure the loan security is still in place and the business is operating in accordance with the loan agreement.



### 3.10 Strategic Enterprise Development Fund

- Only 25% of ENL's total loan and equity portfolio of \$78.2 million is estimated to be recoverable. The remaining 75% is an estimate of the uncollectible accounts and has been provided for in the allowance for doubtful accounts. This estimate is a matter of judgement and the actual collections may be more or less.

#### Findings and Recommendations

#### Measuring and Reporting on Performance

Performance reporting is an important part of public accountability. Recent developments within the Province has placed increased emphasis on public accountability. However, in order for performance reporting to be effective, departments and agencies must clearly define strategic objectives, identify performance indicators, set targets and report actual performance against these targets.

Our review indicated that the Department of Development and Rural Renewal has developed a strategic plan. This plan and other departmental information indicates that the mission of the Department is *"to foster economic development in the twenty economic zones by means of a strong proactive field and corporate support and effective partnerships to marshal resources in support of regionally planned business development and economic diversification"*.

One of the mechanisms for carrying out this mission is the Strategic Enterprise Development Fund which provides equity, loans, guarantees and company development grants to assist small and medium-sized enterprises where the activities are consistent with strategic priorities of the economic zones and the Government. Objectives for this fund have been identified in a number of documents including the Department's Strategic Plan and budgetary submissions. These objectives are also consistent with those established for Enterprise Newfoundland and Labrador Corporation and the proposed new Business Investment Corporation. These objectives are:

- Promoting the values of an enterprise culture and encouraging self-reliance throughout the Province;
- Promoting, especially, small and medium-sized enterprises;
- Promoting and assisting in the integration of local economic development and the work of educational institutions; and



### 3.10 Strategic Enterprise Development Fund

- Developing and implementing programs to provide persons with the information, advice and assistance, both financial and other, needed to facilitate the development of small and medium-sized enterprises.

Prior to December 1998 the Department had no formal performance indicators identified. However, informally, the number of jobs created or sustained was tracked as part of the application for funding by various new and existing businesses. In addition, the amount of funding provided, collections on loans outstanding, and write-offs were also provided when requested.

In December 1998, the Department developed a Strategic Plan which formally identified a number of performance indicators including increased employment, increased employment income, and number of businesses starting up, maintained or expanded; however, the Department has not yet established targets for, or reported on, each of its outcomes. Without targets it is not possible to assess whether performance is below or above expectations.

To date there has been very little formal reporting on the performance of the Department's loan program. Annual financial statements for the loan program are prepared and audited; however, there is no formal reporting to the House of Assembly or publicly on what has been achieved with the funds. Ad hoc reporting has been done in news releases and in Department correspondence.

In response to our 1996 review of ENL, the Department indicated that from the inception of ENL in 1991 through to 1996, approximately \$100 million was invested to create or sustain in the order of 15,000 jobs throughout the Province. In a ministerial briefing in November 1998, the Minister stated that since 1996, approximately 3,500 jobs have been created or maintained at a cost per direct job of \$5,600. According to the Department's statistics, during the past three years, 3,682 jobs were created or sustained. Figure 5 provides a summary of approved projects for the past three fiscal years for each of the five regions.

### 3.10 Strategic Enterprise Development Fund

Figure 5

Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Approved Projects  
1 April 1996 to 31 March 1999

| Region   | Funding (\$ Millions) |               |         | Projected Employment |
|----------|-----------------------|---------------|---------|----------------------|
|          | ENL                   | Other Sources | Total   |                      |
| Avalon   | \$ 6.5                | \$ 36.9       | \$ 43.4 | 1,074                |
| Eastern  | 1.6                   | 1.4           | 3.0     | 304                  |
| Central  | 4.2                   | 12.2          | 16.4    | 1,002                |
| Western  | 5.0                   | 20.1          | 25.1    | 1,035                |
| Labrador | 3.1                   | 4.1           | 7.2     | 267                  |
| Total    | \$ 20.4               | \$ 74.7       | \$ 95.1 | 3,682                |

Source: Department MIS reports

These statistics were gathered from presentations for funding for approved projects. It should be noted that the employment outlined in Figure 5 reflects the employment plans of the approved project and do not represent actual employment created or sustained. Departmental staff indicated that projected numbers can change for a number of reasons, including such things as undisbursed loans, closed businesses, operational delays, and changing markets/business plans.

For example, one company we examined estimated it would create 33 new jobs from its approved project in February 1997; however, as of November 1998 only three employees had been hired. A loan of \$500,000 was provided to another business in September 1998 to create 12 jobs; however, in early 1999 the company ceased operations. Included in the 1999 projected employment total of 1,308 is one project which estimated creating 80 jobs; however, to date, funds have not been advanced by ENL and no employment has been created.

### 3.10 Strategic Enterprise Development Fund

Figure 5

Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Approved Projects  
1 April 1996 to 31 March 1999

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### **3.10 Strategic Enterprise Development Fund**

In addition, it may be perceived that its funding was solely responsible for creating and sustaining that particular job; however, as shown in Figure 5 the Department's funding is normally a small part of the funding package and the cost per job is usually much higher. For example, the Department reported a cost per job of approximately \$5,600 which equates to the Department's cost; however, the total cost per direct job, when considering all sources of funding (including ACOA, HRDC and private sector/commercial) is approximately \$25,800 per direct job.

The Department does not provide an annual report to the House of Assembly on its operations. Financial statements for Enterprise Newfoundland and Labrador Corporation are audited by our Office each year and are included in the Public Accounts of the Province which are tabled in the House of Assembly. However, financial statement information on its own is not adequate information for assessing the operations of the Corporation.

The Director of Portfolio Management prepares a monthly status report which outlines outstanding loan guarantees, the status of the special reserve, and a status of approvals to date compared to budget. Also, in June 1999, the Department prepared an internal report analyzing the investment portfolio stratified by dollar value and by industry sector, along with estimated employment figures and leveraged sources of funding. This report is not required to be prepared on a regular basis and is not provided to the House of Assembly.

#### **Application and Approval**

The assessment and evaluation of an application for funding is an important step in ensuring that the objectives of the loan program will be achieved. Therefore, we would expect to see a business plan including an analysis of market potential, information on competition, financial statements and projections, employment potential, and an analysis of the borrower's ability to repay.

Our review indicated that Department policy requires that a detailed project evaluation be carried out on all applications for funding. The size, nature and complexity of the project will determine the specific information required from the applicant. Our review indicated that, for the most part, the information required and expected was on file and that presentations for funding to the applicable approval authority were prepared on business plans and applications received. Figure 6 identifies the process for providing financial assistance.

### 3.10 Strategic Enterprise Development Fund

Figure 6

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**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Policies and Procedures  
Process for Financial Assistance**

- There must be an application or request for funding from the applicant;
- The Corporation must carry out a proposal evaluation and written assessment of the application and information (financial, management and marketing) provided by applicant;
- Funding (in aggregate) has to be approved as follows:
  - Funding less than \$10,000 can be approved by an economic development officer.
  - Funding up to \$75,000 can be approved by the regional directors.
  - Funding between \$75,001 and \$500,000 must indicate the recommendation of the regional director and be approved by the Corporate Transaction Committee. The approval of the Board of Directors is not required.
  - Funding between \$500,001 and \$1,000,000 must be approved by the Board of Directors and approval is not required by Cabinet.
  - Funding in excess of \$1,000,000 must be reviewed by the Board of Directors, recommended or not recommended for approval, and forwarded to Cabinet for its decision;
- The Corporation must provide an offer of financing, receive a signed letter of acceptance, and put in place appropriate legal agreements; and
- Disbursement of funds must be supported by an approved cheque requisition form.

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Source: ENL Policies

As disclosed in Figure 4, we reviewed the 36 files selected for application/approval review and 6 of the 15 files selected for detailed review. We reviewed these 42 files to determine if the application process was properly supported and evaluated and whether projects met the Department's criteria for funding. These criteria, according to departmental policy, include a demonstration of growth potential, evidence of export or import replacement objectives, and evidence of shareholder and management commitment. Other criteria, disclosed in



### **3.10 Strategic Enterprise Development Fund**

budget documents and program review reports, include having objectives consistent with strategic sectoral priorities, creation or sustainment of employment, non-competitive, provision of net economic benefit, and a lack of conventional funding sources.

For purposes of this report, we have summarized our findings under six aspects of the application and approval process. These are the assessment of business plan, assessment of financial viability, adequacy of security, authorization limits, disbursement of funds, and other funding sources. Our comments are as follows:

#### **1. Assessment of Business Plan**

Most loan files examined contained some form of business plan including a market analysis, financial projections and employment projections. However, in our opinion, a number of assessments were not adequate as significant information was not obtained. In other cases, funding was provided although significant problems were identified. Of the 42 files reviewed, we had concerns with 7 files. For example:

- One proposal required the reprocessing of a raw material, the pricing of which was determined on the open market. As the pricing of this product was directly related to market conditions, the risk of profit or loss was evident. The presentation for funding indicated that a publicly traded United States company would provide necessary engineering drawings worth \$2.0 million for a 20% share in the company and would purchase all of the new company's products. The file indicated:
  - the United States company was experiencing financial difficulties and therefore could no longer be considered as a major customer. However, projected sales were not adjusted to reflect this reality. Projected sales of \$48 million in 1996 were never revised and the \$151 million in 1997 was decreased to \$126 million.
  - the engineering drawings, worth \$2 million, were determined to be out of date or obsolete.

### 3.10 Strategic Enterprise Development Fund

Although this was considered a high risk venture, ENL felt that there was potential for success in the information technology industry. In January 1996, \$1 million was provided to the new company as a term loan of \$500,000 and an equity investment of \$500,000. However, as early as November 1996, ENL suspected that the investment of \$1 million was in jeopardy. As at 31 March 1999, ENL was owed \$1,188,692, including interest receivable. Only \$38,331 was recovered as of the date of our review.

- ENL approved an equity investment of \$100,000 in one company in July 1996 to cover the costs of marketing expenses and asset purchases. This loan was the fourth loan provided to the company since July 1995. In July 1995 a term loan of \$100,000 was provided, in January 1996 a \$56,000 term loan was provided, and in February 1996 a \$50,000 term loan was provided.

Since the start up of the company and up to the time of the \$100,000 equity loan, the company experienced severe cash flow shortages. No sales had been recorded and the previous loans totaling \$206,000 were in interest arrears with no principal payments made to date. A review of the file indicated that an established competitor was already in the market which contributed to the poor sales of the company and its eventual business closure in April 1998. The presence of this competitor was not known or identified during the application process; however, given the competitor's position in the market and liaisons within that particular industry, they should have been considered a major factor. As at 31 March 1999, this client owed ENL \$316,342. The Department is estimating that none of this \$316,342 will be collected.

- A company was provided with a \$100,000 term loan in September 1997 even though there were a number of concerns raised including technical/processing aspects of operations, product supply, management reputation, and a previous ENL associated account which experienced a write-off of \$7,000 on a \$15,000 loan. Commercial operations began in the Fall of 1997; however, no sales have been recorded to date. As at 31 March 1999, ENL was owed \$104,603, including interest receivable.



### 3.10 Strategic Enterprise Development Fund

#### 2. Assessment of Viability

In evaluating businesses which have applied for funding, we would expect the Department to consider previous dealings with the business, payment history and the integrity of management. Based on our review of the 42 files, we had concerns with 7 files relating to the business evaluation. We found that loans were made to businesses that had existing outstanding loan or equity accounts that were in default, were experiencing financial difficulties at the time of funding, or provided evidence that management were not acting in good faith. For example:

- In 1992 one company was provided with a venture capital loan of \$1,000,000 to invest in a second company operating a quarry. In August 1994, an additional \$1,000,000 was invested directly into the second company even though that company had reported losses in 1992, 1993 and 1994 totalling \$1.5 million. Also, in September 1996, ENL guaranteed a \$250,000 loan to the second company which was paid out by the ENL in February 1999. Information on file indicated that the second company reported losses in excess of \$500,000 in 1995 and \$1,000,000 annually for each of 1996, 1997 and 1998. The company closed its operations in August 1998. As at 31 March 1999, both associated companies owed a combined amount of approximately \$2.7 million to ENL.
- From October 1992 to March 1994 a company was advanced two loans of \$500,000 each and the payment on a loan guarantee of \$229,000. During this period, documentation on file indicated that ENL officials had significant concerns over the account including payment difficulties, management non-cooperation, operational problems, poor and risky markets, and a lack of financial information. At this point, the company owed approximately \$1.2 million.

In 1996, the company was also advanced interim contract financing of \$120,000 and \$40,000, and in 1998-99, \$60,300 in term financing was provided to the company even though the earlier loans of \$1.2 million were still in arrears. Although the \$120,000 loan was repaid, as at 31 March 1999, the company owed ENL \$1.9 million, including interest.

### 3.10 Strategic Enterprise Development Fund

In 1998-99, an additional \$700,000 was approved for a related company with the same management team and a dependence on the company for a supply of raw material. Concerns were again raised regarding poor management history, competitive foreign markets, lack of confirmed customers/markets, outdated manufacturing process/equipment, poor financial performance and financial position of the related company who would be the major supplier of raw material, and additional start up costs not included in business proposal. As of our review date, none of the \$700,000 has been advanced as conditions for the loan have not all been met.

### 3. Adequacy of Security

The obtaining of adequate loan security is important in protecting the Province from unpaid loans and investments. Our review of the 42 files identified 4 cases where we had concerns with the level of security taken. In some cases, adequate security was not in place at the time cheques were issued, while in other cases, the value of the security had deteriorated so that it could not provide for any recovery of the loan provided. One case is identified elsewhere in our report and one was recovered in October 1999 through a Federal lending agency. The remaining two examples are as follows:

- In October 1995, ENL provided a \$1,000,000 loan to a company, secured by a first fixed charge on mine and milling machinery and equipment and a shareholder's subordination agreement subordinating shareholder advances to ENL. The shareholder's subordination agreement was signed by all three shareholders in November 1995; however, in a letter dated 22 November 1995, ENL's lawyer stated that they had not received a resolution agreement from the board of the parent company and that the individual who signed on behalf of the board may not have had the authority to sign. ENL's lawyer also informed ENL that "it is possible that the Corporation (major shareholder) could at some point challenge the validity of this Agreement".

Our review of the files at ENL indicated that the company repaid to the shareholders \$500,000 in November 1996, and as a result removed necessary operating cash flows. ENL demanded the repayment of the \$500,000 based upon non-compliance with the agreement; however, the major shareholder stated that the subordination agreement was never authorized by their board and was not legally binding. The company ceased operations at the end of January 1997 and ENL has yet to act upon its charge against the company's machinery and equipment. As at 31 March 1999,

### 3.10 Strategic Enterprise Development Fund

the company owed ENL \$474,676 including interest, all of which is doubtful of collection.

- In July 1998, \$73,400 in interim financing was provided for the financing of a Newfoundland company to create computerized training modules on a contract basis. The loan was secured by an assignment of funds being paid to the Newfoundland company by a contractor who in turn would receive funds from the sale of the product to a major customer.

ENL requested and obtained a copy of the contract between the company and the contractor; however, they did not request a copy of the contract between the contractor and the major customer. Three months after funds were disbursed to the Newfoundland company, ENL became aware that there was never a contract between the contractor and major customer, and as a result the contractor never received any monies under the contract. ENL has had to rely on its security on certain equipment and does not expect to fully recover all monies advanced. As at 31 March 1999, the company owes ENL \$76,800, including interest.

#### 4. Authorization Limits Exceeded

Departmental policy requires cabinet approval for funding in excess of \$1 million; further, the funding authorization limits, as shown in Figure 6, include the aggregate amount of a client's commitment to the Department under current applications and outstanding balances from existing accounts including associates and affiliates. The term associates and affiliates is further defined in the Corporation's policy. Any amendments to an account must also follow the necessary approval process. In addition to the 36 files selected for review of the application assessment process, we also reviewed the 15 files selected for detailed review to ensure authorization limits were not exceeded. The following accounts had loans/equity investments provided which were over \$1,000,000 and there was no evidence on file that Cabinet approval had been obtained:

- One company had a \$1 million venture capital loan approved in 1991-92 which it invested in a related company. This related company subsequently received an additional \$1 million in 1994 without the required Cabinet approval.
- One company was approved loans totaling \$1,368,000 from 1987 to 1989 without the required Cabinet approval.

### 3.10 Strategic Enterprise Development Fund

- One company was approved loans for \$1,269,065, excluding interim contract financing from 1992 to 1996 without the required Cabinet approval. Also, an associated company received approval for \$700,000 during 1998-99 which was not approved by Cabinet.
- Another company was approved \$2.5 million in 1990 and in 1995 \$492,883 in interest was capitalized as an equity investment. Neither of these two transactions were approved by Cabinet.

One component of ENL's funding program is a telefilm industry assistance which is directed toward the film and video industry to provide increased opportunities for Newfoundland-based producers, production companies and film makers. According to ENL's policy directive, assistance is limited to 20% of the total cost for any one telefilm project. A resolution of the Board also limited the maximum contribution to any one project at \$300,000 per year and a maximum allowable outstanding balance (including associates and affiliates) to \$500,000.

On 17 October 1997, the Newfoundland and Labrador Film Development Corporation was incorporated; however, telefilm projects continued to be funded through ENL. It was not until the 1999-2000 Provincial budget that the funding was allocated to the Newfoundland and Labrador Film Development Corporation. As such, any funds distributed through ENL should have complied with directives established by the Board.

Our review of the telefilm industry assistance provided by ENL identified the following:

- One company received \$393,182 in funding over two years, while two associated companies had outstanding balances of \$406,272, thus exceeding the \$500,000 maximum allowable outstanding balance permitted for associated and affiliated companies.
- Another company was approved a loan in November 1997 for \$484,000 which already had an approximate loan balance of \$1,157,000 outstanding, including interest, thereby exceeding the \$500,000 maximum allowable total loan limit. Also, there was no evidence on file that cabinet approval was obtained on the loans that exceeded \$1 million in aggregate to this company.

ENL periodically disburses funds on behalf of its clients in order to protect its interest in the client. Common examples of payments include legal fees or insurance premiums on secured assets. Individuals are invoiced for any payments made and charges are added on to their account as security credits. Our review identified one account where disbursements noted as security credits were improper. \$20,000 was disbursed to one



### 3.10 Strategic Enterprise Development Fund

company in October 1997 as a security credit; however, file evidence indicates the payment was a loan to assist in short-term financing needs. This \$20,000 loan was approved by the CTC in January 1998 when an additional loan of \$55,000 was provided. In May 1998 an additional \$38,000 was disbursed as security credits to cover employee remittances to Revenue Canada and to help the client with severe cash shortages. These two payments were approved by the Manager of Enterprise Services and not by the CTC. All three payments were paid to the client and not to the respective vendor.

ENL provided venture capital loans under its Venture Capital Program and related policies. Funding was provided to registered venture capital companies which in turn provided these funds and an equal contribution to investee companies for an equity position. Because ENL's investment funds were matched by the venture capital company, corporate policy stated that ENL's funding did not have to be secured; however, ENL funding is required to be supported by a venture capital agreement. ENL's funding would be held in trust by its legal counsel until they received support that an equal contribution was made by the venture capital company. ENL policies require that the maximum to be invested into any one investee company is \$500,000 and the maximum to be provided to any one venture capital company is \$1,000,000. The Board has the authority to authorize amendments to these policies as required. Our review of transactions for one venture capital company identified the following:

- This venture capital company received 12 loans totaling \$1,775,825 from 1987 to 1993 which it in turn invested in six different investee companies. The aggregate loans exceeded \$1,000,000 in November 1990. Since November 1990, an additional six loans, totaling \$687,500, were approved and disbursed, none of which were approved by Cabinet as required by corporate policy. Only \$47,000 of the \$1,775,825 has been recovered to date from the venture capital company.
- Disbursements totaling \$200,000 were made to two of the six investee companies in which certificates confirming that the venture capital company had invested its 50% share into the investee company were signed by an officer of the investee company who was also an officer of the venture capital company. This source of evidence did not offer an independent verification that funds were invested into the investee companies.

### 3.10 Strategic Enterprise Development Fund

- In 1995 two of the six investee companies redeemed their shares for a total of \$351,400 which the venture capital company re-invested in another investee company which had previously received approximately \$500,000 in venture money from ENL. By reinvesting this money, the venture capital company exceeded the \$500,000 threshold. We also note that the investee company that received the \$351,400 subsequently went into receivership in 1996 and the venture capital company was forced to write off its investment.
- Corporate policy requires that within six months of the end of its fiscal periods, the venture capital company and each of its investee companies shall provide audited financial statements. The latest financial statement on file for the venture capital company is for the year ended 31 December 1996 and is unaudited. The latest financial statements for two of the four remaining investee companies are audited financial statements for the year ended 31 December 1997, while one investee company has provided an unaudited financial statement for the year ended 31 December 1996. The last financial statements for the other investee company were September 1993 and this investment was written off by the venture capital company in 1997.
- In December 1996, the Board ceased accruing interest on all loans and deferred all loan payments because of a lack of cash flow and the inability of the venture capital company to meet its debt obligations. However, a review of investee companies' financial statements indicated that \$88,745 was paid to the venture capital company or its parent company in 1996 as management fees and administration expense recoveries and \$67,482 was paid to the venture capital company or its parent company in 1997 as management fees and administration expense recoveries.

### 5. Disbursement of Funds

Departmental policy requires that cheque requisitions must be used for each disbursement of funds with supporting documentation such as receipts and invoices to be attached. Our review indicated that all disbursements had an approved cheque requisition on file. However, our review identified two disbursements where supporting documentation was not attached to the cheque requisition to support the payment. These include the following:

### **3.10 Strategic Enterprise Development Fund**

- ENL approved a \$100,000 term loan in July 1997 to a hunting/outfitting operation which was to be used to purchase an aircraft for \$220,000. A review of the file identified a bill of sale for \$1.00 for the purchase of the helicopter. Since our review, the Department was provided with correspondence from its legal counsel that the aircraft was purchased for \$130,000 plus HST. A bill of sale was still not presented to support the purchase.
- In 1990, ENL approved a project for the construction of a hotel at a total project cost of \$6.8 million, of which ENL contributed \$2.5 million. \$650,000 of the project costs were provided to a project management company for management fees and for settling overdue creditors. Evidence on file indicates that ENL was not provided with any support relating to the satisfying of creditors.

#### **6. Other Funding Sources**

One of the criteria for funding by ENL is the applicants must have exhausted other sources of funding. There was no documentation on file in 26 of the 42 files that we reviewed to demonstrate that financing had been sought through conventional lending sources prior to approaching ENL.

#### **Monitoring of Loan/Equity Portfolios**

Loans are classified as grade 1 to grade 4 with grade 1 representing accounts which are current, grade 2 representing accounts which are in arrears and show signs of experiencing problems, grade 3 representing accounts which are in serious financial difficulties which will likely not be overcome in the normal course of business, and grade 4 representing accounts which have been demanded on by the Department. Employees responsible for accounts categorized as grade 1 or 2 are to monitor each account on an ongoing basis. Monitoring is to include a monthly review of the aged accounts receivable listing to ensure accounts are current, periodic review for compliance with underlying conditions, ensuring financial statements are received according to the agreed upon terms, and the annual review and assessment of each account.

To assess how well ENL is monitoring its loan and equity accounts, we looked at five areas which include: how ENL monitors the financial condition of companies that have loans, the extent of personal contact with these companies, how ENL monitors its security on these loans, the circumstances under which security on these loans is relinquished and how well ENL is collecting on amounts owed to them.



### 3.10 Strategic Enterprise Development Fund

Our review indicated the following:

#### 1. Financial Monitoring

The submission of financial statements is critical to the financial monitoring of a company and its account. According to the offers of financing, clients are responsible for submitting financial statements on a regular basis to the regional offices for analysis. Each of the regions reviewed maintained a financial statement compliance report to track financial statements received and outstanding. One region's (Central) compliance report was last dated January 1997, after which time any new clients were placed on a monthly card monitoring system. This process, although adequate for determining financial statements due in any given month, does not provide a quick look at how the entire region's portfolio is complying with financial statements submissions. A summary of the financial statement compliance reports is shown in Figure 7.

**Figure 7**

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**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador  
Financial Statement Compliance**

|                           | <b>Avalon</b> | <b>Eastern</b> | <b>Central*</b> | <b>Western</b> |
|---------------------------|---------------|----------------|-----------------|----------------|
| Accounts listed on report | 280           | 60             | 278             | 258            |
| New or closed accounts    | 51            | 7              | 45              | 44             |
| # of F/S expected         | 229           | 53             | 233             | 214            |
| F/S received              | 120           | 35             | 185             | 201            |
| Current F/S on file       | 12            | 3              | 21              | 32             |

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\* Accounts registered up to January 1997

Source: Regional Financial Statement Compliance Reports

### **3.10 Strategic Enterprise Development Fund**

A review of client files indicated that clients were contacted if financial statements were not received; however, evidence on file showed that client contact was usually once a year. Of the 50 sample files chosen for monitoring review over four regions:

- 17 had financial statements on file for 1997 or subsequent year ends at the time of our analysis;
- 6 did not have any financial statements on file at all;
- 27 had financial statements on file for one or more year ends before 1997; and
- financial statements received were not always date stamped to determine the time span between the year end and submission date. Our review indicated that of the 44 financial statements received, 18 were dated and 6 of these 18 were received after a year had lapsed from the year end.

Without current and accurate financial information it is difficult for the Department to determine the status of its accounts, the existence of any securities held or the future viability of the client.

#### **2. Personal Contact**

Department policy requires regular contact with each client to be maintained by either personal visit or telephone call quarterly in the initial year, annually thereafter and quarterly or more frequently for all accounts other than grade 1 accounts. Of the accounts reviewed for adequacy of monitoring, 21 of the 50 files reviewed had no evidence on file that site visits had been made. Furthermore, 16 of these 50 files did not have any client contact of any sort documented subsequent to 1997. Site visits which were documented in the 29 files were usually limited to one visit since the loan was initially issued. Without regular site visits, the Department is unable to ensure that assets pledged still exist and are adequately valued, that the business is a going concern, and employment figures recorded appear reasonable.

#### **3. Monitoring of Loan Security**

The Department uses various methods of securing its loans. For example, companies may be required to pledge their assets either by way of a chattel/realty mortgage or a fixed and/or floating charge debenture on assets, personal guarantees may be required from directors/owners of companies and there is a requirement for companies to have sufficient insurance. Our review of this area indicated the following:

### 3.10 Strategic Enterprise Development Fund

- **Chattel Mortgages**

Chattel mortgages are basically claims against pledged assets which are registered with the Registry of Bills of Sale, Conditional Sales and Chattel Mortgages every five years. We were informed by each of the regions reviewed that chattel mortgages are monitored closely through monthly chattel mortgage reports. These reports identify outstanding registrations and registrations which are coming due for re-registration. Our review of these reports did not identify any major concerns, except for one instance where a newly approved account was not set up on the report and the chattel mortgage was not registered until eight months after the money had been disbursed. The chattel mortgage was prepared 15 July 1998; however, it was not registered until March 1999. Prior to the chattel mortgage being registered, another chattel mortgage was prepared by a bank and registered on 10 February 1999. This chattel mortgage contained some of the equipment listed on the ENL chattel mortgage.

- **Asset Valuations**

There was little or no evidence on the files we reviewed that actual inspection of property, equipment and furniture held as security were periodically conducted. Although files did record if site visits were made, there was no documentation to confirm whether secured assets were inspected or inventoried. We identified two situations in which action was taken to realize on secured assets; however, upon seizure the assets did not exist. The details of these two instances are as follows:

- In 1994, assets of one company were to be seized; however the assets in question were either scrapped or seized by other creditors. As of 31 March 1999, \$28,836 was outstanding on this account.
- One company was provided with \$60,000 in October 1991 and \$50,000 in September 1993, both secured by chattel mortgages and a personal guarantee for the shortfall in security for \$35,000. In 1995, a notice of demand was issued and ENL attempted to realize on its chattel. Upon seizure of the assets for sale, the client informed ENL that some items on the chattel list never existed, some were property of someone else, some had been damaged and disposed of and some were sold. ENL did not realize any money from the assets under the chattel. Instead it acted

### 3.10 Strategic Enterprise Development Fund

upon the personal guarantee for which it only received \$17,000. During 1998-99, ENL wrote off \$75,620 in principal and interest.

- **Personal Guarantees**

Personal guarantees are sometimes used to strengthen a security position or to supplement a shortage of other securities taken. Eight of the 42 files we reviewed under the application/approval process had personal guarantees taken as a form of security. Our review identified, that as at 31 March 1999, seven of these accounts are graded as category 2 or more and three accounts have 100% of their principal balances in arrears. We also identified two accounts through our monitoring process which have been wound up or are in the process of winding up. One personal guarantee is valued at \$175,000 while the other is valued at \$150,000. As of our review date, no action has been taken to realize on these two personal guarantees.

- **Property Insurance**

ENL requires clients to have property insurance and in case of an insurance claim the loss payable is to ENL. Clients requiring insurance are monitored through reports similar to the financial statement compliance reports and chattel mortgage reports. These reports identify the insurance company, effective dates and expiry dates. Although each region's report formats were not consistent, the reports provided for the necessary information to monitor whether insurance policies are in place. A review of these reports and sample files identified the following concerns:

- The Central region did not maintain a report format but used a manual card system for monitoring insurances. This system, although providing the same level of individual client monitoring, does not provide an overview of how the region is monitoring the insurances of its entire portfolio. A report detailing all clients and their required policy information can be accessed more easily, reviewed by the Regional Manager more effectively, and provide a quick overview of the regions compliance.

### 3.10 Strategic Enterprise Development Fund

- Insurance policies are not always kept up to date and in some cases have not been renewed, even though loan balances are still outstanding and assets have been pledged. Our review of sample files indicated that letters are on file informing the client that insurance policies have expired, and insurance companies are required to notify ENL of policy cancellation or expiration. However, our review of 50 files identified 9 accounts where evidence on file indicated that their insurance policies had not been renewed. One of these companies had an account balance owing as of 31 March 1999 of \$1.9 million, including interest. The insurance policy on file was last renewed in 1994. We note that during 1999, a fire occurred which destroyed their office building which was secured by ENL and in which financial records were destroyed. In the case of property damage or loss, without adequate insurance, ENL's asset securities are in jeopardy and in case of business disruption, ENL's loan repayments may be negatively affected.
- A review of the regional reports identified the Eastern region with 31 clients with expired policies, the Western region with 61 expired policies, and the Avalon region with 107 expired policies. These reports did not identify whether policies were no longer required by ENL or whether clients are now inactive.

#### 4. Relinquishment of Loan Security

ENL may also invest in the equity of a company. The purpose of these equity investments, according to ENL's policy, is to assist companies with significant growth potential to develop a strong capital base and leverage other sources of funding. Equity investment is by way of common shares, preferred shares, and/or shareholders' loan.

ENL's policy indicates that security will be taken on equity investments. Specifically, the policy refers to "*other security as deemed appropriate for shareholders' loans but may rank secondary to prime lenders*". Given these references to security on direct equity investments, it is clear that ENL anticipates security on this type of financial assistance.



### 3.10 Strategic Enterprise Development Fund

Our review of a number of companies provided with term financing which was subsequently converted to equity investment indicated the following:

- Contrary to ENL policy, equity investments are not always being used to assist companies with significant growth potential to develop a strong capital base and leverage other sources of funding. Rather, some companies which have term loans with ENL and which are experiencing significant financial difficulty are having their term loans, which have fixed terms of repayment, converted into equity investments with no fixed terms of repayment.
- When term loans are converted to equity investments, ENL relinquishes either totally or almost totally all security they had in place for the original term loan. As at 31 March 1999 ENL had \$18.7 million invested in the equity of various companies. ENL anticipates that it will not collect any of the \$18.7 million. Our review identified the following loans which were converted to equity positions and had significant security positions given up:
  - Term loans and capitalized interest totalling \$1,150,000 were converted into an equity investment in 1989 and 1996 with no set terms of redemption, with the only fixed security being a \$175,000 personal guarantee and a charge against certain assets on debt not transferred. Securities given up included other personal guarantees and fixed and floating charges against property and other assets.
  - In November 1991, ENL approved a \$2.6 million loan to one company, in which approximately \$2.3 million was drawn down from October 1992 to March 1996 and \$69,000 in interest was capitalized in April 1993. In September 1996, \$1,200,000 in debt was converted into an equity investment in the parent company, \$1,000,000 was received from the parent company of which approximately \$676,000 was applied against principal, interest of \$372,000 was written off and all undistributed funds were cancelled. After this restructuring, the company owed \$1,742,728, including interest receivable to ENL as at 31 March 1999, of which only \$500,000 remained secured under the original fixed and floating charge on all assets of the company.

### 3.10 Strategic Enterprise Development Fund

- ENL provided a \$300,000 term loan to one company in 1989. In 1990, the company went into receivership; however, with a restructuring of the \$300,000 and accrued interest to equity, new term financing of \$295,000 and a \$700,000 loan guarantee through the Department of Finance, the company survived, although it never stabilized. In 1992, ENL converted the \$295,000 term loan and accrued interest to an equity investment. After these loans were converted to an equity investment ENL gave up its security position on the company's property and buildings. In April 1997, the Department of Finance paid out \$771,000 on its loan guarantee. As at 31 March 1999, the outstanding equity and accrued dividends/interest totalled \$1,146,714, excluding the \$771,000 owed to the Department of Finance. There is no security on either the \$1,146,714 owed to ENL or the \$771,000 owed to the Department of Finance.

#### 5. Collection Activities

The Department, through its headquarters and the five regional offices is responsible for monitoring loan collections and taking corrective actions where needed. The following processes are performed to assist in the monitoring and collection of accounts:

- Delinquency reports are submitted to the regions by headquarters each month. These reports are reviewed by the applicable employee to determine what accounts require action.
- Monthly statements are sent to each client from headquarters. These statements detail amounts due and any arrears unpaid.

These procedures are performed whether an account is current or in arrears. However, once an account goes in arrears, Department policy requires that client contact is to be made by telephone or by mail and if not resolved an investigation and account review is to be completed to develop a plan of action to resolve the situation. Our file reviews indicated that letters were originally sent to clients requesting them to address the arrears situation; however, there was little or no evidence that follow-up procedures were regularly conducted if accounts were not brought current after the first contract.



### 3.10 Strategic Enterprise Development Fund

Based on a review of ENL's collection activities and its predecessor agencies since 1979, ENL is collecting approximately 65% of all amounts owed to it. During 1998-99, ENL indicated that it had collected \$5.3 million on its current billings of \$8.2 million while it only collected \$1.3 million on past due amounts of \$21.7 million owing as at 31 March 1998. Currently, only 1 of 10 companies with a loan balance in excess of \$1 million is making any payments on its loans. The repayment is only \$5,000 per month on a \$2.2 million interest-free loan and \$0.5 million equity balance.

Our review identified situations where ENL required representation on the client's board, requested copies of board minutes, and, in one case, appointed Departmental staff as company management and in many cases amended loan terms to ease the financial burden on the client. However, our review also indicated that ENL was reluctant to take legal action to realize on its security positions. The following are examples of situations where accounts have been in arrears for a number of years and actions taken were limited or did not bring the account current:

- One company had its loans consolidated and refinanced in February 1995 bringing the total outstanding at that time to \$380,215. Interest of \$87,203 was capitalized and repayments were set at \$48,655 per annum. Since restructuring only \$62,327, of which only \$10,058 was principal, was received, and no payments had been made in 1998 or 1999. ENL holds first charge on all lands, buildings and equipment.
- ENL approved loans/equity totaling \$1,368,000 from 1987 to 1989 into an aquaculture project. Since that time ENL has capitalized interest of \$604,361, received \$101,788 up to 1994, ceased interest accruals, written off \$545,573, and converted \$685,000 to equity for a company which had little value. The only security of value to ENL is a \$175,000 personal guarantee and a charge over assets (mainly boats and cages) on the remaining loan. The company is currently winding down its operations and assets are being auctioned off which have an appraised value of approximately \$105,000. ENL has contacted the client but no action to date has been initiated on the personal guarantee.
- As at 31 March 1999 one company had a loan and equity balance outstanding for \$2.8 million. This loan was approved in June 1990 at \$2.5 million and increased to approximately \$3.0 million in January 1995 with the capitalization of interest of \$492,000. Since 1990, payment terms have been amended a number of times with the latest terms set at \$5,000 per month plus an annual payment of 10% of sales over \$850,000, commencing with the 31 October

### 3.10 Strategic Enterprise Development Fund

1998 year end. Annual sales averaged \$950,000 over the past 7 years. With this repayment plan, the Department can expect \$70,000 each year, which computes to a pay back period of 40 years. Since the most recent restructuring, ENL has received \$5,000 per month; however, no financial statements have been received to determine if any payments are required based on sales.

- ENL provided loans of \$22,500 and \$47,900 in 1989 and 1992 respectively to one company. The first loan was secured by a chattel mortgage and the second loan by personal guarantees. As of March 1999, no principal payments have been made and no enforcement of securities has been initiated.

#### Recommendations

*The Department should:*

- *improve its accountability processes by reporting on what it has accomplished, in relation to established goals, with the funds provided to Enterprise Newfoundland and Labrador Corporation;*
- *adhere to policies and procedures established for the assessment, approval, and monitoring of loans and investments; and*
- *improve monitoring and collection activities through more timely follow-up of client operations and enforcement of loan conditions.*

#### Department's Response

*The recommendations of the Auditor General are generally consistent with current direction articulated in the Department's strategic and operational plans. In acting on these matters, however, the Department's approach is to maintain a developmental focus in managing its investment portfolio, consistent with the objectives and purpose of the Enterprise Newfoundland and Labrador Corporation Act and the Strategic Enterprise Development Fund (SEDF) itself.*

*The SEDF is designed to assist small and medium sized businesses take advantage of opportunities that offer the potential to expand and diversify the economy and create new jobs. This is especially important in rural areas which have been significantly impacted by the groundfish moratorium and where small business supports are not readily available through the private sector. A particular focus is on stimulating, at an early stage of development, new emerging sectors of the economy that do not have sufficient track-records to attract normal commercial financing.*

### 3.10 Strategic Enterprise Development Fund

*Individual investment decisions are made carefully, but by their very nature they are risk investments and developmental in nature. The Department acts as a patient investor in this same context, unlike the commercial banking sector, and is flexible on repayment terms as individual circumstances may dictate in relation to the business development objective of the program.*

*While financial recovery of investments is an important objective, the over-riding goal is to stimulate new business activity in the province as a means of creating new jobs. From this perspective, if a small business sustains itself, continues to employ people, and helps strengthen the local economy, the investment can be considered a success, even if the financial investment itself may not be able to be fully recovered due to unforeseen circumstances.*

*It is also important to note that the investment policy for the SEDF changed significantly with the creation of the Department in April 1996, with a greater emphasis on smaller investments of under \$100,000 each and more emphasis on the equity needs of small businesses. It is relevant to note, in this regard, that 96% of those businesses that have received funding since April 1996 were still active as of June 1999.*

#### **Financial Overview of Investment Portfolio**

*The financial overview of the portfolio, as presented in Figures 2 and 3, shows the outstanding balance in the portfolio at the dates specified. This is relevant information to help monitor the financial position of the portfolio, but it does not capture any payments on accounts that have been made over time. Nor do the tables isolate the performance of the portfolio prior to and after the creation of the Department when a fundamental shift in investment policy took place. It is also emphasized that the "allowance for doubtful accounts" (i.e. the amount presented as "uncollectible") is an estimate only and is calculated on a conservative or worst case scenario basis by the Department. Historically, actual collections have exceeded the formal "allowance".*

*The table below provides an overview of the financial performance of investments made over the 1979 to 1999 period, including total collections received on historical investments made over this period. This table shows that \$168.8 million or 55% has been collected to date on balances owed of \$306 million, with \$45.1 million or 15% in formal write-offs, and a combined "allowance for doubtful accounts" and write-offs of 38% for the entire portfolio over this period.*

### 3.10 Strategic Enterprise Development Fund

#### *Loan and Equity Portfolio: 1979-1999 (\$ millions)*

| <b>1979<br/>31 March<br/>Balance</b> | <b>1979-99<br/>Loans, Equity<br/>and Interest</b> | <b>Amounts<br/>Repaid</b> | <b>Amounts<br/>Written Off</b> | <b>Doubtful<br/>Allowance</b> | <b>Percent of Amounts<br/>Written Off or<br/>Doubtful</b> |
|--------------------------------------|---------------------------------------------------|---------------------------|--------------------------------|-------------------------------|-----------------------------------------------------------|
| \$22.1                               | \$283.9                                           | \$168.8                   | \$45.1                         | \$72.3                        | 38%                                                       |

*As noted earlier, any financial review of the performance of the portfolio also needs to be balanced against the business development role played by the SEDF. Repayments on the investments are not the sole measure of success.*

#### **Scope of Review**

*As noted earlier, the investment policy related to the portfolio changed significantly with the creation of the Department in April 1996. A representative sample of 36 accounts from that time were selected for review, but also selected were an additional 15 accounts "with larger balances as of March 31, 1998 ... for detailed review". In the Department's view, the 15 accounts are not representative of the portfolio in the post April 1996 period, in so far as an analysis of the application/approval process is concerned. All 15 accounts involve investments over \$500,000, with 10 of them over \$1 million. As noted in the report, only 3 investments in excess of \$500,000 each have been made since the creation of the Department. One of these investments was an interim financing arrangement for a federal-provincial cost-shared project which was subsequently fully recovered from that source. A second investment was provided as a short-term "security" guarantee, the full amount of which is expected to be recovered by March 31, 2000. The third approval was a \$700,000 conditional investment which has yet to be disbursed because the conditions have not been met by the applicant.*

#### **Measuring and Reporting on Performance**

*The Department generates formal monthly status reports on investments made throughout each year as well as regular formal reports on the status of the entire portfolio. A major review of the total portfolio was conducted as part of the program review process in 1997 and another major review was completed in mid-1999 on investments made since the creation of the Department. This latter review revealed, among other things, the 96% "survival rate" for businesses assisted. The Department's current strategic and operational plan includes specific actions to build on these reviews and monitor performance outcomes more fully.*



### **3.10 Strategic Enterprise Development Fund**

#### ***Application and Approval Process***

*The key issue to consider, from the Department's perspective, is whether the nature and level of investment risk is understood and taken into consideration in reviewing and deciding on an application. It is not unusual for some information to be lacking or some issues to be completely unresolved as decisions are made. Provided that the matters are duly acknowledged, responsibly considered, and balanced against other pertinent decision-making factors relating to the business development objectives of the program, or otherwise addressed through appropriate conditions of approval, the decision-making process can be considered to be sound. This is the manner in which all investment decisions are taken.*

*It must also be acknowledged that not all investments will succeed, financially or otherwise, for reasons that cannot be foreseen at the time of decision and which may be beyond the control of the business itself. Examples are evident in the report, but this does not necessarily mean that the process is fundamentally flawed.*

*As noted earlier, a distinction also needs to be drawn between the 15 larger files selected for review and the sample reviewed following the creation of the Department. In this regard, the Department notes again that 96% of those businesses that received funding since April 1996 were still active as of June 1999.*

*The Department is also of the view that the documentation presented in the report on some specific cases, both in respect of examples in which it is suggested that weaknesses exist in the application/approval process and in other areas, does not provide a full accounting of all the relevant factors applied in each decision, as documented on each such file, or how any outstanding issues were ultimately addressed in the decision-making process. This leads to an incomplete picture of some of the investment decisions referenced in the report, particularly in relation to the developmental objectives of the program.*

#### ***Assessment of Viability***

*Prior credit history is an important consideration in the investment decision-making process, but does not constitute automatic rejection of an application. File documentation clearly indicates, in all assessments, whether the Department has had any prior experience or dealings with the applicant. This analysis is taken fully into account during the decision-making process, as are other pertinent decision-making factors relating to the developmental nature of the program. All material facts cited in the report pertaining to prior credit histories on specific files were fully documented and taken into careful consideration when the particular investment decisions were made.*

### **3.10 Strategic Enterprise Development Fund**

#### ***Adequacy of Security***

*Availability of security is an important factor in making an investment decision. The specific concerns cited in the report relate to difficulties in executing agreed upon security decisions as opposed to a failure to take due account of security considerations in the decision-making process. As well, of the four specific cases of concern noted in the report regarding inadequate security, one of these investments was recovered in full.*

#### ***Authorization Limits Exceeded***

*The Enterprise Newfoundland and Labrador Corporation Act does not limit the authority of the Corporation in respect of loan amounts. However, a 1994 Cabinet directive does address this matter in that it limits the Corporation to \$1 million for a single individual investment, unless otherwise approved by Cabinet. Prior to 1994, the limit for any single investment or single applicant in a single year was \$4 million. The 1994 Cabinet directive does not limit the Corporation in terms of cumulative investments over time, nor in respect of accumulated balances, nor in respect of associated companies. The Corporation itself established internal policy governing these specific matters, but flexibility has been applied if the requisite internal authorities are obtained for any exceptional circumstances.*

*With one exception referenced in the report (dealing with an improperly authorized advance under a security account), the Corporation was aware of the pertinent circumstances of all files the report references and acted within its authority at all times, taking individual situations into account vis-a-vis the application of internal administrative policy. The telefilm investments, in particular, relate to circumstances subsequent to the establishment of the Newfoundland and Labrador Film Development Corporation wherein government decided to give greater priority to this sector of the economy and increased the annual telefilm budget from \$250,000 to \$1 million. ENL continued to administer the program on a transitional basis, on behalf of the Film Development Corporation, pending the establishment of an acceptable accountability structure and capability within that Corporation.*

#### ***Monitoring of Loan/Equity Portfolios***

*Following significant restructuring of the Department in 1997 as a result of the program review process, a new approach to account monitoring and follow-up was put in place. This posed a greater challenge than originally contemplated and has only recently become fully operational. An internal review is presently underway to evaluate the overall situation and take*

### **3.10 Strategic Enterprise Development Fund**

*appropriate measures to ensure there is adequate attention paid to ongoing account monitoring at all times in accordance with established administrative policy. A significant part of the situation relates to the absence of appropriate file documentation on follow-up activity and monitoring at the time of the audit, as opposed to an absence of actual monitoring or follow-up. This issue will receive particular attention during the review process. Another significant issue relates to the enforcement of property insurance requirements for secured assets where clients cancel or otherwise allow such policies to lapse after the initial investment is made. While the current monitoring system captures when this occurs, the review noted above will address possible means and interventions to deal with this situation.*

#### ***Relinquishment of Loan Security***

*The conversion of a loan to an equity position does not, in and of itself, violate the policy objective associated with equity investments. Proposals for conversions are thoroughly evaluated against the business development objectives of the SEDF and are approved only if they meet same. All proposals are given careful consideration as to their individual circumstances and consequences, including the impact on security positions held. However, by definition, most conversions bring with them the subordination of security in order to achieve the business objective at hand. In the Department's view, all conversions have been diligently applied in relation to the business development objectives of the program, and have been fully in keeping with established administrative policy.*

#### ***Collection Activity***

*As noted earlier, a review is presently underway on ongoing account monitoring practices. This review also includes an analysis of collection performance, within the context of the Department's role as a patient (developmental) investor. It should be noted, however, that action to seize secured assets is usually taken as a measure of last resort where the business is not likely to succeed and where the taxpayers' investment is at extreme risk. The over-riding developmental objective is to work with clients in an effort to make their businesses successful - not to cause the business to fail by premature action on collections or security arrangements.*



### 3.11 Strategic Enterprise Development Special Reserve Fund

#### Introduction

In March 1997 Government transferred \$10 million to the Department of Development and Rural Renewal's Strategic Enterprise Development Fund. This amount was in addition to the regular amount of \$8.1 million allocated during the budgetary process. The additional \$10 million was transferred to the Enterprise Newfoundland and Labrador Corporation and was intended to strengthen the Department's overall small business development efforts over the short term.

As indicated in the *Enterprise Newfoundland and Labrador Corporation Act*, the objectives of the Corporation are as follows:

- (a) promoting the values of an enterprise culture and encouraging self-reliance throughout the province;
- (b) promoting, especially, small and medium-sized enterprises including private businesses, co-operatives, credit union and community development corporations;
- (c) promoting and assisting in the integration of local economic development and the work of educational institutions; and
- (d) developing and implementing programs to provide persons in an area of the province having an interest in participating in the development of small and medium-sized enterprises with the means of accessing information as to the opportunities for that development together with information as to the advice and assistance, both financial and other, available to facilitate that development.

The Enterprise Newfoundland and Labrador Corporation has established policies which define the process which must be followed when approving financial assistance to businesses. This process is outlined in Figure 1.

### 3.11 Strategic Enterprise Development Special Reserve Fund

Figure 1

**Department of Development and Rural Renewal  
Enterprise Newfoundland and Labrador Corporation  
Policies and Procedures  
Process for Financial Assistance**

- There must be an application or request for funding from the applicant;
- The Corporation must carry out a proposal evaluation and written assessment of the application and information (financial, management and marketing) provided by applicant;
- Funding (in aggregate) has to be approved as follows:
  - Funding less than \$10,000 can be approved by an economic development officer.
  - Funding up to \$75,000 can be approved by the regional directors.
  - Funding between \$75,001 and \$500,000 must indicate the recommendation of the regional director and be approved by the Corporate Transaction Committee. The approval of the Board of Directors is not required.
  - Funding between \$500,001 and \$1,000,000 must be approved by the Board of Directors and approval is not required by Cabinet.
  - Funding in excess of \$1,000,000 must be reviewed by the Board of Directors, recommended or not recommended for approval, and forwarded to Cabinet for its decision;
- The Corporation must provide an offer of financing, receive a signed letter of acceptance, and put in place an appropriate legal agreement;
- Disbursement of funds must be supported by an approved cheque requisition form; and
- After providing financial assistance, the Corporation must carry out monitoring activities including on-site visits, submission of financial information and financial statements.

### 3.11 Strategic Enterprise Development Special Reserve Fund

The \$10 million was considered a special reserve fund and the nature of the funding differed from the normal capital funding provided through the Enterprise Newfoundland and Labrador Corporation. Most of the funds provided under this fund were in the form of forgivable loans or investments based upon employment created. During the fiscal years 1997-98 and 1998-99 the full \$10 million and an additional \$1,975,000, provided in 1998-99, was allocated to various projects as disclosed in Figure 2.

#### Scope and Objectives

The objective of our review of the special reserve fund was to determine whether the assistance provided from this fund was adequately approved, monitored and in accordance with the objectives of the program.

In performing this review, we examined three projects approved under this fund and specifically the procedures followed in assessing, approving and monitoring them.

Figure 2

#### Department of Development and Rural Renewal Strategic Enterprise Development Fund Special Reserve Fund Status of Fund 31 October 1999

| Project                                  | Approved Amount      | Date Disbursed   | Amount Disbursed    | Amount Undisbursed |
|------------------------------------------|----------------------|------------------|---------------------|--------------------|
| BPS Call Centre                          | \$ 800,000           | 20 August 1997   | 800,000             | 0                  |
| Payments under Guarantee-BPS Call Centre | 55,188               | 3 July 1998      | 55,188              | 0                  |
| Advances-BPS Call Centre                 | 34,040               | 27 May 1998      | 34,040              | 0                  |
| Cabot Call Centre                        | 1,000,000            | 28 November 1997 | 1,000,000           | 0                  |
| Wood Products International              | 350,000              |                  | 0                   | \$350,000          |
| Newfoundland Bonding & Composites Ltd.   | 9,500,000            | Note 1           | 9,500,000           | 0                  |
| Unallocated                              | 235,772              |                  | 0                   | 235,772            |
| <b>Total</b>                             | <b>\$ 11,975,000</b> |                  | <b>\$11,389,228</b> | <b>\$585,772</b>   |

Note 1: Disbursements totaling \$9.5 million made at various times from 23 November 1998 to 6 October 1999.

### **3.11 Strategic Enterprise Development Special Reserve Fund**

#### **Conclusion**

The Department of Development and Rural Renewal administers the Strategic Enterprise Development Fund and through this fund provides assistance to small and medium size businesses. Over 90% of the \$11,975,000 in the Special Reserve Fund was provided to three companies. There are stated objectives for the fund and standard procedures to be followed in assessing, approving and monitoring assistance provided to businesses through this fund. Our review disclosed that these procedures were not followed for the three projects that we reviewed under the Special Reserve Fund of \$11,975,000. For example:

- Although the Department of Development and Rural Renewal, through Enterprise Newfoundland and Labrador Corporation, was responsible for the disbursement of the funds, it had very little to do with the assessment, approval and monitoring of the three projects that we reviewed under the reserve fund. The Department of Industry, Trade and Technology was responsible for the call centre projects and the subsequent monitoring of these projects, while the Department of Finance was responsible for Newfoundland Bonding & Composites Limited. It was evident from our review that these projects were pre-approved before the Board of ENL or the Department became involved.
- Our review of three approved projects funded through the reserve fund indicated that they were not subject to the policies and procedures as established for other loan and equity investments. Thorough assessments were not performed, verification of business plan assertions was limited and monitoring was inadequate.

#### **Findings and Recommendations**

The Department of Development and Rural Renewal, although responsible for the reserve fund of \$11,975,000 million, was only marginally involved in the application, assessment and approval of the projects. The Department of Development and Rural Renewal's responsibility was limited to some loan assessment, Board approval and cheque disbursement. The Board's approval was either given after funds had been disbursed or agreements had been entered into and public announcements made. Figure 3 outlines the significant dates for each major project.

### 3.11 Strategic Enterprise Development Special Reserve Fund

Figure 3

**Department of Development and Rural Renewal  
Special Reserve Fund  
Chronology of Events**

| Description              | BPS Call Centre                | Cabot Call Centre              | NBCL             |
|--------------------------|--------------------------------|--------------------------------|------------------|
| Department               | Industry, Trade and Technology | Industry, Trade and Technology | Finance          |
| Initial funding          | \$800,000                      | \$1.0 million                  | \$9.5 million    |
| Business plan date       | 30 July 1997                   | 28 October 1997                | 29 May 1998      |
| Presentation for funding | 27 November 1997               | 27 November 1997               | None             |
| Board approval           | 27 November 1997               | 27 November 1997               | 17 November 1998 |
| Funds Disbursed          | 20 August 1997                 | 28 November 1997               | Various          |
| Cabinet Approval         | N/A                            | N/A                            | 16 July 1998     |
| Agreement signed         | Not Dated                      | 18 November 1997               | 12 November 1998 |

The three projects that we reviewed under the reserve fund were provided with funding through forgivable loans or investments based upon future employment created. The two call centres' loans are forgiven at a rate of \$1,667 for every person year of employment created. This equates to \$.95 per hour of employment created. Newfoundland Bonding & Composites Limited investment is to be redeemed at a rate of \$9,500 for every person year of employment created. This equates to \$5.22 per hour of employment created.

### 3.11 Strategic Enterprise Development Special Reserve Fund

#### BPS Imaging Partnership

On 19 July 1997 the Government announced that a portrait studio was establishing a 48 seat call centre in St. John's which would provide 160 full-time jobs, to provide sales and appointment scheduling services for the portrait studios in 60 retail stores across Canada. The call centre commenced operations in September of 1997 and ceased operations on 15 May 1998, in total operating in Newfoundland for 8.5 months. Total funding received by it from the Special Reserve Fund was \$889,228. Our review indicated the following:

- The BPS Call Centre was incorporated in Newfoundland on 29 July 1997 as 10620 Newfoundland Limited, with two equal shareholders, both being companies which were resident in Ontario.
- The approval process for the \$800,000 conditional loan was not in accordance with the normal approval process followed by Enterprise Newfoundland and Labrador Corporation. For example:
  - The owner of one of the two shareholder companies of 10620 Newfoundland Limited had approached the Government for financial support for a call centre which resulted in a letter being sent, on 10 July 1997, from the Department of Industry, Trade and Technology, confirming that the Province would provide a contribution of \$5,000 per job to be paid in advance as a forgivable loan, totalling \$800,000. However, up to that time no business plan had been submitted and no investigation or assessment had been performed.
  - The \$800,000 was disbursed in full on 20 August 1997, although the Board of ENL did not approve the loan until 27 November 1997.
- The evaluation of the application dated 30 July 1997 for funding from the Department of Development and Rural Renewal identified concerns about several issues. These concerns included the lack of confirmation of the financial strength of the proponents, and of what was referred to as "the related company", a portrait studio, lack of confirmation of the \$508,000 promised shareholders' investment, the lack of substantiation of the projected sales increase of the call centre from \$5.6 million in year one to \$10.4 million in year three compared to a reported current



### 3.11 Strategic Enterprise Development Special Reserve Fund

sales of the portrait studios of \$7.5 million, and the degree of dependence on the portrait studios agreement, which had not been provided. Despite these concerns, the funds were advanced in full without any resolution of these issues.

- The assessment refers to a reported relationship ongoing since 1989 between the proponent and the proponent's partner, operating portrait studios in 60 retail stores across Canada, under a licence agreement from the national retailer. The alleged licence agreement was not reviewed and no independent verification of any of the representations of the proponent was undertaken. In fact, after the call centre's financial difficulties came to light, the proponent's partner advised that he had no relationship with the proponent prior to being approached by him after the Newfoundland Government funding was promised.
- No written agreement was ever provided between the call centre and the portrait studio, and, after the call centre was in financial difficulty, it was learned that no written agreement had ever existed.
- The \$508,000 initial shareholders investment promised by the business plan, about which concern was noted in the assessment, was not made.
- Although the entire project had been assessed as though it was a call centre in Newfoundland, operating separate and distinct from the portrait studios, with its revenues being described as a percentage of gross sales of the portrait studios, in fact there had been no separation of finances nor records between the call centre and the 58 portrait studios. Therefore, the Newfoundland call centre had been operated as part of one entity with the portrait studios (none of which were situated in Newfoundland) under the trade name BPS Imaging Centre.
- Although the call centre was described as a separate entity from the portrait studios throughout the funding approval process, the 2-year cash flow and profit and loss statements provided with the application clearly showed costs of the portrait studios so it should have been obvious that the call centre would be operating as an integral part of the portrait studios.



### 3.11 Strategic Enterprise Development Special Reserve Fund

- Despite the recognized dependency of the call centre on the portrait studios, no investigation of the profitability or financial strength of the portrait studios operation was conducted.
- The only remedy for the Government to recover the loan, after all the funding was advanced on 20 August 1997 was "to require the company to re-pay," with no security whatsoever. Although the purpose for the loan was to equip and furnish the call centre in St. John's, no security over that equipment and furniture was taken, and no verification of its costs, or ownership, was required.
- The \$800,000 forgivable loan was to be forgiven at the rate of \$1,667 per person year of employment provided, defined as 1,750 hours of work per person year. Since there was no security taken for the loan, if the call centre failed, as it did, there was no way to recoup any of the "unearned" portion of the \$800,000.
- The call centre claimed to have provided 153,729 hours of the 840,000 hours needed to forgive the full \$800,000. As a result, the Province forgave \$146,437 of the \$800,000 loan and wrote off the remaining \$653,563. However, the 153,729 hours were never certified by external auditors, as required by the agreement.
- The Province also provided a loan guarantee of \$200,000 on 8 May 1998 after the company was in serious financial difficulty, subject to the condition, among others, that "the appropriate officers of the company" execute a promissory note. No promissory note was ever obtained and Government has determined that the \$55,188 paid out under the guarantee will not be recovered from the company.
- The company was also provided with \$95,000 on 27 May 1998 to cover 75% of unpaid wages for employees of the company. Government subsequently received \$61,000 of this amount on 29 June 1998 resulting in a net contribution from Government of \$34,000.
- Government paid \$63,648 in October 1998 to an accounting firm to carry out a review of the operations of the company. This review indicated numerous concerns including the following:
  - Since the financial records of the call centre and the portrait studios were not segregated, it could not be determined if the Government funding was used for the call centre.

### 3.11 Strategic Enterprise Development Special Reserve Fund

- The accounting records were neither complete nor current. The bank accounts were not reconciled on a timely basis, account information was incomplete, accounts were posted improperly and some transactions were not posted at all.
- There was no documentation of site visits to the call centre by Government officials to monitor the use of government funds. The \$800,000 was disbursed based on notification from the shareholder that a rental agreement had been entered into for operating space. There was no documentation of site visits to determine if the centre was functioning as identified in the business plan. We note, however, that Government officials made a site visit to the call centres' parent company's head office in Ontario on 23 January 1998 to discuss financial and operational concerns.
- No annual audited financial statement was received because the call centre did not remain operational for a full business cycle.

#### **Cabot Call Centre**

The Cabot Call Centre was incorporated in Newfoundland on 23 October 1997 as 10642 Newfoundland Limited. Its purpose was to raise money for charities and obtain magazine renewals. The proponent, who operated two call centres in New Brunswick and one in Ontario for the same purpose, stated that those centres were at maximum capacity and needed to expand. This is the same individual who proposed the BPS Call Centre. Our review identified the following:

- The Agreement to provide a \$1.0 million forgivable loan was signed 13 November 1997, and announced 14 November 1997; although the project was not approved until 27 November 1997 by the Board of Directors of Enterprise Newfoundland and Labrador Corporation. Therefore, the normal approval process for the loan was not followed.
- Disbursement of the \$1.0 million was conditional upon confirmation that the company had signed/negotiated a lease. However, the \$1.0 million was disbursed, in full, on 28 November 1997, upon provision of an offer to lease signed by another company owned by the proponent. An offer to lease signed by another company of the proponent does not fulfil the condition of the disbursement of the \$1.0 million.

### 3.11 Strategic Enterprise Development Special Reserve Fund

- In January 1998 the \$1.0 million was held in the bank account of the other company of the proponent in Toronto, and not by the Cabot Call Centre Limited, with whom Government had made the agreement.
- The \$1.0 million is a forgivable loan, with no security, forgivable at a rate of \$1,667 for every 1,750 hours of work, equivalent to \$5,000 for every full-time job created and maintained for three years. If the call centre fails, the Province will have no means of recovering the unforgiven part of the \$1.0 million investment. As at 31 March 1999 this amount was \$817,079.
- No confirmation of the financial condition of the owner was obtained.
- The \$1.0 million in funding was disbursed without the Province receiving any support whatsoever for the projected revenue, such as copies of telemarketing contracts or confirmation of their existence from third parties.
- Other than a letter from the major shareholder and proponent, there was no confirmation that the required \$710,000 investment by the shareholder had been made.
- The presentation for funding stated a requirement for \$710,000 for capital equipment with the only other cost being wages. No confirmation was provided of the \$710,000 cost, and the entire \$1.0 million was disbursed before the lease commencement date with no verification of expenditures for equipment. Although security over the equipment could have been required, none was sought and the Province's only remedy in the event the call centre does not fully earn the loan is to "require re-payment" from the company with no security whatsoever.

Furthermore, the unaudited financial statements for the year ended 30 November 1998 indicated that the cost of capital assets was only \$252,000.

- There was information on file of the number of call stations set up and computer systems on hand but no proof of their cost or ownership. As of 20 May 1998, almost 6 months after opening, it appeared that 24 call stations had been installed, half the number called for in the business plan.

### **3.11 Strategic Enterprise Development Special Reserve Fund**

- The operations of the call centre have not been adequately monitored. There was no evidence on file to indicate that site visits to the call centre were made. However, we do note that a site visit was made to the call centre's parent company's head office in Ontario on 23 January 1998 to discuss financial and operational concerns.
- A review of file information also indicated that periodic employment figures were provided by the client. These employment figures were certified by the company's auditor as required by the agreement.
- Unaudited financial statements for the year ended 30 November 1998 indicates that the company is in poor financial condition and has not recorded any revenues for that year other than Government grants of \$293,000.

#### **Newfoundland Bonding and Composites Limited**

Newfoundland Bonding and Composites Limited, a wholly owned subsidiary of Canadian Helicopters Limited, was established in July 1998 to provide manufacturing, repair and engineering services for aircraft components. The Government of Newfoundland agreed to contribute \$9.5 million towards a total estimated cost of \$20.5 million for the construction and start-up of this manufacturing facility.

In exchange for the \$9.5 million, the Government received 95,000 redeemable preferred shares in the company at a par value of \$100 per share.

The agreement between Government and Newfoundland Bonding and Composites Limited entitles the company to redeem, at nominal value, 9,500 preference shares for every 100 person years of employment provided by the company during the first six years of operation, based on the premise that 1,000 person years of employment would be created within the first six years of operation. The company's auditors are required to certify the calculation of the amount redeemed.

If Newfoundland Bonding and Composites Limited does not meet that job creation target by its sixth anniversary of operation, Government has the right to convert each unredeemed preference share to a common share, provided it does so within 180 days after the sixth anniversary, failing which the company retains its right to redeem the preference shares at nominal value.

### 3.11 Strategic Enterprise Development Special Reserve Fund

Our review of the Province's procedures for approving funding for this project indicated the following:

- The approval process for the \$9.5 million investment was not in accordance with the normal approval process followed by Enterprise Newfoundland and Labrador Corporation. For example:
  - there was no presentation for funding to the Board of Directors of Enterprise Newfoundland and Labrador Corporation as is normally the case for loans greater than \$500,000;
  - the project was not approved by the Board of Enterprise Newfoundland and Labrador until 17 November 1998 which was after the project received Cabinet approval on 16 July 1998;
  - the agreement between Government and the company was signed on 12 November 1998, before the Board of Enterprise Newfoundland and Labrador Corporation approved the project on 17 November 1998; and
  - although there were numerous issues identified when the business plan was initially received, these were not all resolved; however, the project was approved.
- Information on file indicated that Government was considering providing financial assistance of \$7.0 million for the construction of a building to compensate the corporation for the incremental costs associated with establishing a business in Gander since the company already had access to a building in PEI. However, although the initial proposal referred to the \$7.0 million for the construction of a building and all documentation available supported this, Government provided \$9.5 million in financial assistance. Government officials subsequently informed us that the \$9.5 million related to the acquisition of equipment and tooling, and not the building. Figure 4 outlines the original estimated project cost and the revised estimates.



### 3.11 Strategic Enterprise Development Special Reserve Fund

Figure 4

#### Estimated Project Costs (\$ Millions)

| Item                  | Original Project Cost Estimate | Original Proposed Government Funding | Revised Project Cost Estimate | Final Government Funding |
|-----------------------|--------------------------------|--------------------------------------|-------------------------------|--------------------------|
| Land and Building     | \$7.0                          | \$7.0                                | \$7.0                         | \$0                      |
| Equipment and Tooling | \$7.6                          | \$0                                  | \$9.5                         | \$9.5                    |
| Working Capital       | \$1.5                          | \$0                                  | \$4.0                         | \$0                      |
| Total                 | \$16.1                         | \$7.0                                | \$20.5                        | \$9.5                    |

Source: Departmental files

- Except for total estimated costs indicated in Figure 4, there were no details on what comprised the estimated project cost of \$20.5 million. There was no substantiation for the projected building cost of \$7.0 million which the Government initially considered funding and no comparative quotes were required by Government. The only evidence on file at the Department of Finance to support the \$9.5 million which Government officials indicated was provided for equipment and tooling was a listing of equipment totalling \$7.4 million and related invoices totalling \$6.3 million.

As a result, Government did not assess the estimated cost of the building or equipment and tooling to determine if it was reasonable in support of the request for funding.

- Government did not have any independent external verification of either the status of the building construction or estimated costs to completion. Instead, funds were disbursed based on the passage of time and evidence by way of letter from the company constructing the building that everything was on schedule.
- The Province's security on its \$9.5 million equity investment is a first fixed charge on tooling and equipment at or prior to delivery and installation and a floating charge on all assets upon completion of construction of the building. Our review of the security debenture indicated that some of the equipment listed was not specifically identified (e.g. no serial number indicated). The

### 3.11 Strategic Enterprise Development Special Reserve Fund

floating charge on all assets ranks behind security given for term financing for the building and any operating credit.

- The Agreement requires the parent company to provide a shareholder's loan of \$1.5 million and a \$2.5 million dollar equity investment. The Agreement includes a postponement of claim against the \$1.5 million shareholder's loan (i.e. the loan cannot be repaid until all of Government's preferred shares are redeemed). However, the \$2.5 million equity investment is not subject to a similar postponement of claim.
- The estimates of the number of jobs to be created by this project varied significantly between the period May 1998 and July 1998 without any explanation as to why the estimates were changing over a short period of time.

The "Executive Summary" of the Newfoundland Bonding and Composites Limited proposal, dated May 1998, stated that there would be 40 person years of direct employment during the construction phase, and 20 person years at commencement of production, rising to 75 "in the medium term," plus five administrative persons. Notes of a meeting between the company and Government representatives on June 1998 refer to a job creation estimate of 30 post construction, increasing to more or less 85 after five years of core business, and comments that "the cost per job from a government perspective, is problematic." Another document on file dated June 1998 describes employment estimates as being 30 at start-up moving to 70 if five-year growth projections are realized. However, the job creation estimate became 1000 man years in six years, based on annual increments of 50 jobs, to 250, over a six-year period, in July 1998.

- Monitoring activities have included 3 site visits by Department officials and receipt of a listing of equipment purchased to April 1999. In addition, the Department has received correspondence from the building construction engineer and the applicants legal counsel indicating status of the project. However, no documentation of actual building costs has been received.

#### **Response - Department of Development and Rural Renewal**

*The purpose of the Special Reserve Fund (SRF) was to strengthen Government's capacity to foster the growth of small and medium sized enterprises that could not reasonably be accommodated with the normal annual budget of the Strategic Enterprise Development Fund.*



### 3.11 Strategic Enterprise Development Special Reserve Fund

*All projects approved under SRF were consistent with these purposes and in keeping with the objectives of the governing legislation, the Enterprise Newfoundland and Labrador Corporation Act.*

*The three projects selected for review by the Auditor General can be characterized as investment prospecting projects. Specific financial investments were deemed necessary in each case to attract the business activity to the province. Other jurisdictions were offering similar or equivalent incentives to attract the business opportunities and it was judged in the public interest to make an intervention in an effort to locate them in this province.*

*The financial incentives for the two call centres were established at the equivalent of \$5,000 per job under the terms and conditions comparable to those available in other competing jurisdictions. The incentive provided to NBC was intended to offset the cost of establishing that enterprise in an alternative jurisdiction and, in doing so, create 250 new jobs and stimulate the development of a new industry within the province.*

*The nature of these investments, as investment prospecting incentives, dictated a different approach to assessment, decision-making and monitoring than investments historically made under the Strategic Enterprise Development Fund. This accounts for the involvement of several departments and the application of different administrative procedures and policies governing the investments.*

*The Board of Directors of the Enterprise Newfoundland and Labrador Corporation acted within the mandate, authority and discretion granted to it under the ENLC Act in dealing with the three projects in question.*

*The BPS Call Centre failure was triggered by extenuating and unforeseen events beyond the control of the company (i.e. the 1998 ice storm in Quebec/Ontario) that caused a severe and unrecoverable cash-flow crisis within it. The Cabot Call Centre and NBC remain fully operational and are generally on schedule relative to the original business plans and targets for new job creation.*

*Subsequent to the funding provided to the above three projects, and in particular following on the failure of the BPS Call Centre, the Departments of Development and Rural Renewal, Industry, Trade and Technology, and Finance reviewed the issues concerning the process of approving any further funding which may be available from the Special Reserve Fund. It was agreed that such funding should be dealt with in the future through a strengthened assessment and approval process.*

### **3.11 Strategic Enterprise Development Special Reserve Fund**

#### ***BPS and Cabot Call Centres - Department of Industry, Trade and Technology***

*To fully understand and appreciate the province's efforts to build this sector especially as it relates to the first two centres to establish in the province, it is important to have all the information. The following points are raised to clarify and add to the information provided by the Auditor General.*

*In 1995 the province, through the Department of Industry, Trade and Technology, entered into a partnership agreement with NewTel Enterprises Limited to form NETWORK Newfoundland and Labrador. NETWORK was assigned the mandate to develop and execute a dedicated, strategic and proactive approach to encouraging new business investment in the call centre industry, thereby generating employment opportunities for the residents of Newfoundland and Labrador. Each opportunity is assessed on its own merits by NETWORK and EDGE staff.*

*Prior to making the decision to provide financial assistance to BPS Imaging, and subsequently CABOT Call Centre, an evaluation of the company's business plan was conducted and the business credentials of both principals were assessed. It was determined that one principal possessed more than 30 years experience in film processing and had a long-standing relationship with the Hudson's Bay Company. Prior to any disbursement of funds by the province, this relationship was verified in a letter from the Hudson's Bay Company referencing an additional five year extension on a licence agreement that had been in existence with the principal since 1989. The second principal demonstrated 10 years experience in call centres, operating successful facilities in two other provinces. Business Information reports generated by Dun & Bradstreet confirmed the financial stability of this principal's existing company.*

*The principal assets of a typical call centre are computer equipment and related software. The resale value of such assets is acknowledged in the industry to be insignificant in relation to its original cost. The risk of having no security was an acknowledged factor in concluding the deal. This deal was part of an effort to establish the province as a serious contender for call centre business. The province has accomplished this goal with the addition of Cabot Call Centre with its 170 employees and two subsequent centers that collectively employ more than 150 people. The end result is the launch of a new industry, and a significant increase in the level of interest by other companies to locate in the province.*

#### ***BPS Imaging Partnerships - Department of Industry, Trade and Technology***

*While it is acknowledged that a final agreement between the partners on the specifics of how the partnership would work was not provided, a letter*

### 3.11 Strategic Enterprise Development Special Reserve Fund

*of agreement in principle, signed by both parties, was submitted as part of the business plan.*

*It was always known and acknowledged that the call centre was providing a service to the Bay Portrait Studios which were operating in numerous Hudson's Bay Stores across Canada. There is nothing unusual about this. In fact, the nature of the call centre business is such that the call centre is oftentimes remote from the core business activity and operated as a separate business entity.*

*The Auditor General suggests that no site visits were made to either monitor use of funds or determine if the centre was functioning consistent with the business plan. In fact, subsequent to its decision to establish a call centre in the province, BPS Imaging received ongoing recruitment and implementation support from the province through NETWORK. From August to December 1997, NETWORK assisted BPS Imaging with its recruitment efforts to ensure success in meeting proposed time frames. NETWORK also facilitated discussions between BPS Imaging and local telecommunications, computer, and furniture providers, and witnessed the delivery and installation of call centre stations, computer, telephone lines and automated call dialing equipment. During this time, BPS Imaging also received several site visits by senior Industry, Trade and Technology officials. Continuous contact between the province and the principals of BPS Imaging Partnership was maintained throughout the company's nine months of operation.*

*The \$508,000 investment by the shareholders was not tied to any particular schedule or time line. In fact, it was agreed that the investment could be put back into the operations from the internally generated funds of the call centre. A subsequent review of the operations by the accounting firm of PriceWaterhouseCoopers disclosed that the shareholders had contributed \$1.4 million to the operations up to the time it ceased operations. The review also confirmed the numbers relating to the hours of work provided and the loan forgiveness.*

*On May 5, 1998 an agreement was entered into with BPS Imaging Partnership and 10620 Newfoundland Limited to provide an interim loan guarantee to enable the company to continue operations and meet its payroll pending the finalization of its restructuring plan. To meet the company's May 8, 1998 payroll it was agreed that funds would be released under the guarantee notwithstanding the fact that all security documentation was not yet in place. With the closure of the operation effective May 18, 1998 the security documentation was not finalized. Nevertheless, government did pursue the repayment of this obligation through legal channels with the Department of Justice.*

### **3.11 Strategic Enterprise Development Special Reserve Fund**

*While the PriceWaterhouseCoopers report acknowledged that the financial records were not in good shape, it also reported that their procedures showed no presence of any illegal activities.*

#### ***Cabot Call Centre - Department of Industry, Trade and Technology***

*NETWORK facilitated start-up and implementation of CABOT Call Centre, again coordinating with the appropriate furniture, computer and telecommunications vendors as required. As with BPS Imaging, CABOT Call Centre received ongoing site visits by both NETWORK and other provincial personnel.*

*While it is acknowledged that CABOT Call Centre did not ramp up as quickly as outlined in its business plan, the centre today has in excess of 48 workstations and employs a total of 170 people.*

*The financial support provided by the Province was neither earmarked nor tied to the purchase of capital equipment. The \$1 million investment was to be used for general operations and forgiven based on the number of hours of work achieved.*

*Under the terms of our agreement with the company respecting "Reporting and Monitoring" the company is required to report annually to the Minister including a certification outlining the number of hours of employment it has provided over the period. The company has complied with this requirement.*

*Although concerns were raised regarding the financial health of the company, the fact of the matter is that the company has been in operation for two full years employing approximately 170 people. It is not unusual for individuals/companies that operate a number of subsidiary operations to format their internal financial statements to meet their own particular requirements.*

*Although the lease was not signed by CABOT Call Centre, it was signed by the parent company which is not an abnormal occurrence in a parent-subsidiary relationship.*

#### ***Newfoundland Bonding and Composites - Department of Finance***

*The Department of Finance does not believe that the calculation of the hourly rate of loan or investment forgiveness (\$0.95 per hour for call centres vs. \$5.22 per hour for NBC) is meaningful, especially if one considers that there would be a significant difference in the skill levels required for the jobs at each project, and hence the salaries paid for the positions. The control period for the call centre projects was also different (three years) than for NBC (six years). In addition, the investment in NBC*



### 3.11 Strategic Enterprise Development Special Reserve Fund

*related to the acquisition of equipment and tooling and was not based upon an amount per job created.*

*Figure 3 suggests that there was no document available for presentation for funding approval to the Board of ENL. This is inaccurate. A memorandum describing the project and the funding program, including a draft copy of the agreement with NBC, was provided to and discussed at an ENL Board meeting on November 17, 1998. Following this presentation, the Board authorized the disbursement of the funds.*

*The comment that there were numerous issues identified and not all were resolved is in reference to a document prepared by a Department of Development and Rural Renewal official upon initial review of the company's business plan. This document was prepared to facilitate discussion on the business plan with the company, and it would not be unusual for some issues to be unresolved and some questions unanswered even after this process.*

*Providing financial assistance of \$7.0 million for the construction of a building was one of several earlier options discussed with Government. Another option which was put forward was for Government to cover 100% of the cost of equipment and tooling, initially projected at \$7.6 million. Government subsequently approved \$9.5 million which was tied to higher employment levels, requiring increased levels of equipment and tooling costs versus the original estimates. The Auditor General notes that the company had access to a building in another province. This other location was a major issue in discussions with NBC. Clearly, this Province was anxious to acquire the project, and through negotiations was successful in landing this important facility for the benefit of the Province, and particularly the central region. Government's contributions to the revised project cost (\$9.5 million out of \$20.5 million) was not significantly greater, proportionately, than the proposed contribution to the original project cost (\$7.0 million out of \$16.1 million).*

*There is evidence, other than statements by Department of Finance officials, that Government's \$9.5 million contribution was provided for equipment and tooling. This is contained in the security document where it is provided that the Province's floating charge on all assets, which is in addition to its fixed charge on equipment and tooling, will rank behind the security given for any term financing subsequently arranged for the building, and any operating credit.*

*The Department of Finance has on file a listing for equipment in excess of \$9.0 million. As for the comment that some of the equipment listed in the security debenture is not identified with, for example, a serial number, this is not unusual for customized equipment or for equipment such as a sanding or painting booth that is fixed to the premises.*

### 3.11 Strategic Enterprise Development Special Reserve Fund

*No funding was provided specifically for the construction of the building and, therefore, independent external verification of the status of the building was not deemed necessary. Contractor's certificates verifying that the project was on schedule, as well as occasional site visits by Department of Finance officials were sufficient. The funding was disbursed in accordance with a timetable outlined in the company's request for financial assistance and contained in the November 12, 1998 agreement. Evidence of expenditures or progress billings were not required. However, before each advance to the company, Government did require, among other things, evidence that the project was on schedule and that the parent company had made proportionate advances on its shareholder's loan and equity investment.*

*CHC Helicopter Corporation ("CHC") holds all of the issues and outstanding shares in Newfoundland Bonding and Composites. As a condition of the financial assistance provided to NBC, Government requested and obtained from CHC a "best efforts" assurance that NBC's business plan will be implemented and the company will be successful. In light of this undertaking, it would not be in the interest of CHC to jeopardize the operations of NBC by seeking repayment of their equity investment while Government's preferred shares are outstanding.*

### 3.12 The Enterprise Network Inc.

#### Introduction

The Enterprise Network Inc. is a Crown corporation which was established to make commercial, technical and industrial information equally accessible to individuals and organizations in urban, rural and remote regions of the Province. In addition to its head office in St. John's, much of the Corporation's activities were conducted in five telecentres located in Trepassey, Clarenville, Baie Verte, Stephenville, and Forteau. These telecentres provided clients with access to information technology and related products to assist them in applying the technology to their business and economic needs.

In October 1997, the Corporation closed its telecentres and effectively ceased operations. In September 1998, the Lieutenant-Governor in Council authorized the Minister of Industry, Trade and Technology to dissolve the Corporation. At the date of our review in September 1999, this had not occurred.

Approximately \$1.9 million in capital expenditures were made by the Corporation from its inception in 1991 through 31 March 1999, with the majority (\$1.5 million or 79%) of these expenditures being made prior to 1995. The expenditures related to the acquisition of office furniture and equipment together with an extensive inventory of computer hardware and software. Figure 1 provides details of the Corporation's capital expenditures.

**Figure 1**

**The Enterprise Network Inc.  
Capital Expenditures  
Year Ended 31 March**

| Year  | Capital Expenditures |
|-------|----------------------|
| 1992  | \$ 850,487           |
| 1993  | 264,636              |
| 1994  | 362,199              |
| 1995  | 243,293              |
| 1996  | 142,922              |
| 1997  | 26,032               |
| 1998  | 11,021               |
| 1999  | 0                    |
| Total | \$ 1,900,590         |

Source: Audited Financial Statements



### **3.12 The Enterprise Network Inc.**

During its operations, the Corporation received financial assistance totaling \$11.9 million through operating grants provided under the Federal/Provincial Strategic Regional Diversification Agreement and the Canada/Newfoundland ACOA/Enterprise Network Cooperation Agreement. Funding under these agreements was cost shared 70% by the Government of Canada and 30% by the Provincial Government. The Corporation's one outstanding common share was initially held by the Enterprise Newfoundland and Labrador Corporation; however, effective 1 April 1995, this share was transferred to the Minister of Industry, Trade and Technology. The Corporation's affairs were managed by a Board of Directors appointed by the Minister of Development and Rural Renewal, as agent for the Minister of Industry, Trade and Technology.

#### **Scope and Objectives**

Over the past few years, I have included several items in my annual report to the House of Assembly relating to the lack of controls over capital assets, including computer equipment, in government departments, Crown agencies, school boards and health care boards.

The Enterprise Network Inc. ceased operations in 1997 and decided to transfer its capital assets to various government departments, Crown agencies and community groups. Since the Corporation had spent \$1.9 million in capital assets since 1991, we reviewed the controls over the disposition of its assets.

We completed our review in September 1999 and our objective was to determine whether there was adequate control over the disposition of the assets of the Corporation when it ceased its operations in 1997.

#### **Conclusions**

The Enterprise Network Inc. commenced operations in 1991 and closed its head office and five telecentres in 1997. Over the seven year period, the Corporation had spent approximately \$1.9 million on capital assets. When the Corporation closed in 1997, it decided to distribute its capital assets to various government departments, Crown agencies and community groups. Our review indicated the following:

- 1) The Corporation did not maintain adequate records on its capital assets and as a result, the Corporation could not provide us with a listing of assets that should have been on hand when it ceased operations in October 1997.
- 2) As a result of the inadequate records on capital assets, the Corporation could not indicate exactly what was the final disposition of its capital assets totalling \$1.9 million.

### 3.12 The Enterprise Network Inc.

- 3) Although there were listings prepared for assets transferred to government departments and Crown agencies, the listings were deficient in that there was no cost information provided which would relate these assets back to the total assets of \$1.9 million.
- 4) The Corporation did not maintain listings of the individual assets and their costs which were distributed to each of the community groups. After our enquiry, the Corporation contacted some of the community groups and obtained asset listings. However, these listings were not independently prepared by the community groups and appeared to be photocopies of listings prepared by the Corporation at various dates prior to or during October 1997. Such listings included references to assets as "missing" or being located at employees' homes.

#### Detailed Findings

When the Corporation commenced operations in 1991, it did not develop a policy relating to the control of capital assets. As well, no system was established to identify specific assets and their location. Periodic verification of the capital assets was not conducted, and adequate procedures did not exist to record the addition, transfer and disposal of capital assets.

Although some records were developed by the Corporation and the telecentres in 1995, a complete capital assets sub-ledger was not maintained. Listings developed and maintained by the Corporation's head office and telecentres in 1995 were used to record assets on hand at that time, with no evidence of assets acquired, transferred or otherwise disposed of to that date being identified. As well, our review disclosed several duplicated entries. There were also no indications in the listings as to the dollar value of assets recorded which would relate these assets back to the total assets of \$1.9 million.

Our review of the listings also indicated that some contained only computer related assets. Correspondence between officials within the Corporation revealed there were problems identified with the inventory records relating to computer equipment and that a request was made for listings to be prepared reflecting an accurate count of such equipment.

Our review of capital asset listings indicated that some assets were transferred between the various Corporation sites without full documentation as to identifiers, and that some transfers were not being reflected on applicable listings. As well, some of the assets on the listings were indicated as "missing" or being located in employees' homes with no indication as to attempts to recover these assets. Other cases were identified where correspondence within the Corporation identified assets which were either not recorded on the listings or recorded improperly.

### 3.12 The Enterprise Network Inc.

Departmental officials contend that documentation was available reflecting all assets on hand at various Corporation locations when the Corporation ceased operations in October 1997. We do not accept the Department's position in this regard for a number of reasons. In particular: some of the listings maintained were not dated or were dated prior to October 1997; some listings reflected that individual assets were "missing" or were located at employees' homes; and since continuous capital asset records were not maintained since 1991, the Corporation cannot know whether the lists are a complete and accurate reflection of assets which should have been on hand.

The Corporation's telecentres closed during 1997. Many of the assets located at the telecentres were distributed to various government departments, Crown agencies and community groups. The Corporation did not maintain listings of the individual assets and their costs which were distributed to each of the community groups. After our enquiry, the Corporation contacted some of the community groups and obtained asset listings. However, these listings were not independently prepared by the community groups and appeared to be photocopies of listings prepared by the Corporation at various dates prior to or during October 1997. Such listings included references to assets as "missing" or being located at employees' homes.

#### **Department's Response**

*It is clear that adequate capital asset records were not established and maintained by Enterprise Network Inc. during its period of accountability to the Economic Recovery Commission from inception in 1991 to March 1996 when the newly created Department of Development and Rural Renewal assumed responsibility for it. Due to this situation, it was not possible for the Department to trace all assets acquired since 1991 nor relate them back to their original costs. However, documentation on all assets that were on hand at the time of operational dissolution of the Corporation in October 1997 is on file with the Department.*

*Every effort has been made by the Department of Development and Rural Renewal to ensure, under the circumstances, that the capital assets acquired by Enterprise Network Inc. are duly accounted for in relation to their intended public purpose. In particular, steps have been taken to formally document that any and all assets in possession of former employees were properly returned to the Corporation. This documentation is now on file for all such assets.*

### **3.13 Provincial Post Secondary Awards Program**

#### **Introduction**

Government, in 1998 announced a \$4,000,000 provincial post secondary awards program over a two year period, intended to provide awards to post secondary students based on academic merit and financial needs. This Program is intended to provide a bridge to the new \$2.5 billion Canada Millennium Scholarship Program which commences in 2000. The Provincial Post Secondary Awards Board was established in May 1998 to formulate awards criteria and general administrative procedures regarding the program. Awards were available to students who obtained a student loan from the Department of Education which was insufficient to meet all of their assessed financial need, and who meet the following criteria:

- student awards are available only to students who attend Memorial University of Newfoundland (including the Marine Institute) and College of the North Atlantic and who:
  - are enrolled full time at the institution;
  - have completed at least one semester at one of the institutions; and
  - are in good academic standing.
- students are eligible to receive between \$500 and \$1,000 per year based on their unmet financial need as determined by the Student Loan Program; and
- students are awarded 50% of their unmet financial needs to a maximum award of \$1,000. However, students will only receive awards if they have unmet financial needs of at least \$1,000 (i.e. \$500 award).

As at 31 March 1999, 1,601 students received awards totalling \$1,254,885.

#### **Scope and Objectives**

We completed our review of the Provincial Post Secondary Awards Program in April 1999 to determine whether the Department has established administrative policies and procedures regarding the delivery of the program and whether there was compliance with these policies and procedures.

#### **Conclusions**

The Department has no documented policies and procedures with respect to the delivery of the provincial post secondary awards program and there is no evidence that the established eligibility criteria were ever approved by the Provincial Post Secondary Awards Board.

### 3.13 Provincial Post Secondary Awards Program

There are weaknesses in the process which the Department is following to determine the amount a student is entitled to receive. We found numerous and significant errors in amounts awarded to students as a result of the timing of the award calculation.

Significant issues raised at the Provincial Post Secondary Awards Board meetings have not been addressed by the Board in a timely manner. For example, the time the reports should be produced to determine the amount of an award, the establishment of an appeals process, and the establishment of institutional sub-committees have yet to be resolved.

#### **Findings and Recommendations**

The Provincial Awards Program is monitored by the Provincial Post Secondary Awards Board which was established by the Department of Education to develop award eligibility criteria and administrative procedures regarding the delivery of the Awards Program. Board membership consists of representatives from the Department of Education, Memorial University, College of the North Atlantic, and various Student Bodies. Our review of the Awards Program included a review of Board minutes, established policies and procedures, as well as related processes and systems. Our review also included an examination of 45 of the 1601 awards granted between November 1998 and 23 March 1999. Our review indicated the following:

- There are no documented policies and procedures regarding the delivery of the Awards Program and as a result we had to determine the process through discussions with a number of staff. We also experienced difficulty determining exactly when the awards should be calculated. This is significant since the date the award is calculated can affect the dollar amount of the award as a student's unmet need may increase or decrease throughout the year. Reports used to generate information required to determine student eligibility are currently run on an ad-hoc basis.
- The \$4 million awards program is restricted to students who attend Memorial University of Newfoundland and the College of the North Atlantic. Of the \$4 million, it was intended that 70% would be allocated to Memorial University of Newfoundland and the remaining 30% would be allocated to the College of the North Atlantic. We could not determine the rationale for restricting the awards to these public institutions, or the rationale for the allocations of 70% and 30%.



### 3.13 Provincial Post Secondary Awards Program

- The awards eligibility criteria state that *"students with an unmet need of \$1,000 or more will be awarded 50% of their unmet need up to a maximum award of \$1,000 per year. Awards will range from \$500 to \$1,000"*. A student's *"unmet need"* can change throughout the course of an academic year as a result of a loan reassessment and/or a new loan application. Currently, once an award has been made during the academic year, there is no system in place to ensure that award is adjusted for subsequent changes in the student's *"unmet need"*.

Our review indicated that in 12 of the 45 cases reviewed, the student award was in excess of what the student would have received had the award been granted at 25 March 1999. In another 12 cases, the student award was less than the amount that the student would have received had the award been granted at 25 March 1999. The number of award discrepancies ranged from \$16 to \$695 per student.

This is a concern since some students are receiving awards they are not entitled to and some students are not receiving awards that they are entitled to. For example, students granted an award early in the academic year of less than \$1,000 are not being considered for further awards (to bring them up to maximum annual award of \$1,000) later in the academic year if their *"unmet need"* increases. In addition, if the student's *"unmet need"* decreases as a result of loan reassessment, there is no system to collect the possible over-award.

- In a Board meeting dated 10 March 1999, the board stated *"there would be no separate appeals process necessary because there is currently a financial appeals process at Student Aid and an academic appeals process at the institutions"*. In an earlier meeting, the Board indicated that it would require an independent appeals process. We question the decision of the Board in this instance since Student Aid and Institutions do not administer the awards program and their appeals process does not reflect the way appeals are currently being handled for the awards program. In addition, students who disagree with their award are not referred to the financial appeals process at Student Aid or the academic appeals process at the Institutions. Rather, students who disagree with their award, or who received no award, have their inquiries directed to the Department of Education where they are usually dealt with over the phone.

### 3.13 Provincial Post Secondary Awards Program

- no action has been taken with respect to the establishment of institutional sub committees for the purpose of making award decisions based on eligibility criteria as established by the Board. At the 17 June 1998 meeting of the Board, it was decided that the Board's institutional representatives would provide a listing of the committee memberships at the next Board meeting. This has not happened.

#### **Recommendations**

*Eligibility criteria for the Post Secondary Awards Program should be approved by the Board.*

*Procedures regarding the delivery of the awards program should be documented and approved by the Board.*

*The impact of the loan reassessment process on the timing of awards should be reviewed by the Board with a view towards determining the appropriate timing of awards.*

#### **Department's Response**

*This program will be discontinued after the 1999-2000 fiscal year as it was introduced as a two-year bridging program to the Canada Millennium Scholarship Foundation.*

*The Provincial Post Secondary Awards Program was administered by a committee consisting of representatives from Memorial University, College of the North Atlantic and the Department of Education; in addition three students representing the student unions of each institution and the Newfoundland and Labrador Federation of Students are members of the Board.*

*The Department provided the Board with the flexibility to establish policies and procedures with respect to the delivery of the provincial post secondary award program. These policies and procedures were developed by the Awards Board.*

*The amount of award a student can receive is based on their assessed need through the student aid process. Given the normal fluctuations in an individual's need assessment throughout an academic year, it is not unusual to have situations where the award the student receives may be incongruous with assessed need at some other point during the academic year. Taking this into account, a specific eligibility date was chosen for 1999.*



### **3.14 Deferred Bursaries**

#### **Introduction**

Prior to the introduction of the Newfoundland Student Loan Program in 1994-95, the province administered a Deferred Bursary Program which was intended to offset student debt which was borrowed under the Canada Student Loan Program. This program provided students, who qualified, with bursaries which were deferred until the student consolidated their Canada Student Loan at the bank for purposes of repayment. The bursaries are paid out when the student begins to repay their Canada Student Loan. As at 31 March 1999, there were approximately 7,900 students still entitled to receive approximately \$6.0 million in deferred bursaries which were approved prior to July 1994.

#### **Scope and Objectives**

We completed our review of the Deferred Bursary Program in April 1999. We reviewed the outstanding bursaries as at 31 March 1999 and the Department's plan to disburse these bursaries.

#### **Conclusions**

We found that the Department does not have procedures in place to ensure that all students are paid the \$6.0 million in bursaries they are eligible to receive. A significant number of annual notifications mailed to students in 1998 advising them of their outstanding deferred bursaries, were returned to the Department marked undeliverable. Currently, the Department has no plans to address the undelivered notifications or the large number of deferred bursaries still outstanding.

#### **Findings and Recommendations**

Our review indicated that, as at 31 March 1999, there were approximately 7,900 students entitled to \$6.0 million in deferred bursaries and that payments of deferred bursaries over the past two years have decreased considerably. Figure 1 outlines deferred bursary payments owing over the last seven years ending in March 1999.

Discussions with officials at Student Aid also indicated that since no deferred bursary application has been received and processed since 1993-94, it is highly likely that the majority of students have consolidated their Canada Student Loan at the bank for purposes of repayment and are now entitled to receive their deferred bursary.

Students are not coming forward to collect their bursaries. Officials at Student Aid indicated that approximately 33% of the 8,000 annual notices forwarded to students in 1998 reminding them of their outstanding bursary, were returned undeliverable. Currently, Student Aid has no plan in place to deal with the undelivered notifications and the outstanding bursaries.

### 3.14 Deferred Bursaries

Figure 1

Deferred Bursaries Payable  
Years ended 31 March  
(\$ Millions)

| Year ended<br>31 March | Amount |
|------------------------|--------|
| 1993                   | \$16.7 |
| 1994                   | \$12.2 |
| 1995                   | \$ 9.8 |
| 1996                   | \$ 8.3 |
| 1997                   | \$ 7.2 |
| 1998                   | \$ 6.5 |
| 1999                   | \$ 6.0 |

Source: Financial Statements of the Province

#### Recommendation

*The Department should conduct a review of outstanding deferred bursaries to determine which students are currently eligible to receive their bursaries. Procedures should be established to ensure these bursaries are paid to eligible students.*

#### Department's Response

*The Department of Education does have procedures to pay out deferred bursaries. The procedures, however, are conditional on the student making application for the bursary.*

*The General Information And Application Guide 1999-2000 page 20 and 21 refers to the Deferred Bursaries procedures.*

*In addition, the Department of Education made every possible effort to correspond with students through letters, to advise of deferred bursary eligibility. However, given that the program was completed by 1993, letters were returned undelivered because students had moved and the Division did not have forwarding addresses.*

### 3.15 Loan Remission Program

#### Introduction

The Department of Education administers a Loan Remission Program through its Student Aid Division. The Loan Remission Program was announced by the Province in 1994-95 coinciding with the introduction of the Newfoundland Student Loan Program in 1995 and the earlier termination of the Deferred Bursary Program (see Item 3.14 of this Report) in 1993. However, students were not eligible to commence applying for a loan remission until September 1997. The Loan Remission Program is intended to encourage students to pursue their post-secondary education in Newfoundland and to complete their program of study in a timely fashion by offering a debt forgiveness incentive to students who borrow.

Loan Remissions are provided to borrowers who qualify in accordance with established loan remission criteria as outlined in Figure 1.

**Figure 1**

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#### **Loan Remission Program Basic Eligibility Criteria**

To qualify for loan remission on Newfoundland Student Loans, the applicant must meet the following criteria:

- Apply within 90 days of graduation.
- Graduate from a designated program of study at least 80 weeks in length within or, in certain conditions, outside the province. In addition, programs beyond the initial 80 week program which are determined to advance the student in their field of study will also qualify even if they are less than 80 weeks.
- Graduate within the normal program period length plus a grace period of one academic year.
- Have a combined Canada Student Loan and Newfoundland Student Loan debt of at least \$22,016.

### 3.15 Loan Remission Program

A student who completes an approved academic program within a year of the normal scheduled completion date and has a combined debt (Canada Student Loan and Newfoundland Student Loan) in excess of \$22,016 will have the excess debt paid by the Province. While the Canada Student Loan and the Newfoundland Student Loan debt is used in the calculation of the loan remission amount, the loan remission is applied only to loans issued under the Newfoundland Student Loan Program. Figure 2 provides an example of how the loan remission is calculated.

The success of this program depends largely on the Department's efforts to inform students when they begin and continue through their program of study as to the eligibility criteria they must meet in order to qualify for a loan remission at the end of their program of study.

As of 31 March 1999, the Department approved 661 loan remissions totalling approximately \$3.5 million. Of the \$3.5 million, \$900,000 was paid in 1997-98 and \$2.6 million was paid in 1998-99.

Figure 2

#### Loan Remission Program Calculation of loan remission

Student X has completed a two year diploma program from a private training college and has accumulated \$16,500 in Canada Student Loans (\$165 per week for 100 weeks) and \$11,000 in Newfoundland Student Loans (\$110 per week for 100 weeks). Student X has met all the basic eligibility criteria of the Loan Remission Program. The loan remission is calculated as follows:

|                                     |                 |
|-------------------------------------|-----------------|
| Eligible Canada Student Loans       | \$16,500        |
| Eligible Newfoundland Student Loans | <u>\$11,000</u> |
| Total Eligible Student Loans        | \$27,500        |
| <br>Debt threshold *                | <br>\$22,016    |
| Amount of loan remission            | <u>\$ 5,484</u> |

\* Debt threshold is calculated as the greater of:

- \$22,016 for programs of study between 80 and 128 borrowing weeks; or
- \$172 per borrowing week times the total number of borrowing weeks for programs of study exceeding 128 borrowing weeks.

### **3.15 Loan Remission Program**

#### **Scope and Objectives**

We completed our review of the Loan Remission Program in April 1999. Our review included an analysis and review of policies and procedures for the Loan Remission Program for the academic years 1997-98 and 1998-99 up to 31 March 1999. The objective of our review was to determine whether the Department had established administrative policies and procedures regarding the delivery of the Loan Remission Program and whether there was compliance with these policies and procedures.

#### **Conclusions**

Although the Loan Remission Program was announced by Government in 1994, the eligibility criteria were not finalized and conveyed to students until the 1997-98 academic year. As a result, students enrolled in programs prior to the 1997-98 academic year may have been unaware of the criteria they would be required to meet in order to qualify for a loan remission on completion of their program of study. It is unfair to require students to comply with criteria that they were not aware of at the time of their studies and which had yet to be finalized. It is possible that some students who did not meet the graduation period eligibility criterion would have made a concerted effort to complete their academic programs within the appropriate time frames if they had known this at the time they were pursuing their studies.

The Department was not applying its criterion of requiring students to submit their loan remission applications within 90 days of completing their studies. As a result, we found instances where, because the Department relaxed its loan remission application deadline criterion of 90 days, it was unable to process all loan remission applications in a timely manner and forward them to CIBC within the required 180 day time frame necessary to avoid being charged the 5% risk premium.

It is possible that students who did not meet the 90 day application deadline would have applied if they had known that the Department had relaxed the deadline criterion of 90 days.

We found instances where the Department failed to process loan remission applications in accordance with established guidelines. Of the 38 loan remission applications reviewed, 9 did not meet all of the established guidelines. In one case, a student was awarded a loan remission of \$5,225 although the student did not meet the established criteria.



### 3.15 Loan Remission Program

#### Findings and Recommendations

Our review of the Loan Remission Program included a review of systems and processes and compliance with the Loan Remission Guidelines. Our review also included an examination of 38 of 1,227 loan remission applications between September 1997 and March 1999. Our review indicated the following:

- Although the Loan Remission Program was announced by government in 1994, the eligibility criteria were not finalized and conveyed to students until the 1997-98 academic year. As a result, students enrolled in programs prior to the 1997-98 academic year may have been unaware of the criteria they would be required to meet in order to qualify for a loan remission on completion of their program of study.

This delay by the Department in finalizing and conveying the eligibility criteria was problematic in that one of the criteria requires that *"Graduation must have occurred within the number of study periods normally specified for completion of the program of study by the educational institution, plus one additional period of study."* Our review indicated that several students did not complete their studies within the required time frame. Specifically, our review of 17 rejected loan remission applications indicated that in 12 instances the borrower was refused a loan remission because they did not complete their program of study within the required time frame. Seven of the 12 rejected borrowers exceeded the required study completion period by only one semester while the other 5 borrowers exceeded the required study completion period by two semesters.

Although the Department did not finalize and convey the eligibility criteria until 1997, it is determining a student's compliance with the criteria from 1994 onward. As a result, it is unfair to require students to comply with criteria that they were not aware of at the time and which had yet to be finalized. It is possible that some students who did not meet the graduation period eligibility criterion would have made a concerted effort to complete their academic programs within the appropriate time frames if they had known this at the time they were pursuing their studies.

- Section 2(g) of the Agreement Regarding Student Loans between the province and CIBC states that it is a provincial responsibility to ensure that loan remission payments are paid to CIBC by the 180<sup>th</sup> day following the Period of Study End Date of the applicable borrower. If the loan remission payments are paid to CIBC within the 180 days, the Province does not have to pay a 5% risk premium on that portion of the loan. If the loan remission payments are not

### 3.15 Loan Remission Program

paid by the province within the 180 days, it is not entitled to any adjustments to, or reimbursement of the corresponding portion of the Risk Premium. In order to process loan remissions within the 180 day time frame, the Loan Remission Guidelines state that *"Borrowers should apply for Loan Remission on their Newfoundland Student Loans within 90 days of their final Period of Study End Date."* However, Student Aid has not been enforcing this deadline because many students are/were "unaware" of the existence of the Loan Remission Program.

Our review of 38 of 1227 loan remission applications indicated that in 21 instances, the student did not apply for the loan remission within the 90 day deadline. In only one case did the Student Aid Division reject the application because it was not received within 90 days. In this case, the student appealed this decision and was subsequently awarded the remission due to the confusion surrounding the 90 day deadline. Of the 38 applications received, 20 were approved, 17 were rejected and 1 was still in the process of being reviewed.

Our review indicated that as a result of not applying the 90 day application deadline criterion, many loan remission amounts were not forwarded to CIBC within 180 days of the borrowers period of study end date. As a result, the Province was required to pay the 5% risk premium on these loans.

Our review of the 20 approved loan remissions indicated that in 10 instances the remission did not get forwarded to CIBC within 180 days of the borrowers period of study end date. As a result, the province was charged a 5% risk premium by CIBC at a total cost of \$2,889 for these 10 loan remissions. Of the 10 instances where the remission did not get forwarded to CIBC in time, we determined that the delay could be attributed to the following reasons:

- in 5 of 10 cases, the loan remission application was not received within 90 days of the study end period;
- in 4 of 10 cases, there was an appeal of the original loan remission decision and this delayed the loan remission processing; and
- in 1 of 10 cases, there appears to be no apparent reason for not getting the loan remission to CIBC within 180 days.



### 3.15 Loan Remission Program

- The Loan Remission Guidelines state that the borrower can appeal a loan remission refusal "in writing within 30 days of refusal". The 30 day time frame is in place to ensure that Student Aid can process the appeal and still forward a loan remission to CIBC within the 180 day risk premium deadline, should the appeal be approved. Borrowers are advised of their right to appeal in the loan remission refusal letter; however, they are not advised that they have only 30 days to do so.

Our review indicated that 11 of 23 applications initially rejected for loan remission were subsequently appealed. Of the 11 loan remission appeals, 5 were not submitted by the student within the required 30 day time frame, but were processed by the Student Aid Division anyway. Of the 5 appeals that were not received from the borrower within the 30 day time frame, 4 were approved. In all 4 cases, the loan remission was not forwarded to CIBC within the 180 day time frame. As a result of the Student Aid Division's failure to properly notify borrowers of the deadline for submitting an appeal and its subsequent failure to enforce this deadline, loan remissions approved under appeal could not be forwarded to CIBC in sufficient time and the Province was required to pay the 5% risk premium.

- the Loan Remission Guidelines state that in order for a borrower to qualify for a loan remission, they must meet the stated eligibility criteria. Our review indicated that in 9 of the 38 students sampled, the Student Aid Division failed to determine loan remissions in accordance with the stated eligibility criteria as follows:
  - for 3 students the loan information was not properly verified;
  - for 1 student, there was no evidence in the file that the borrower had completed their program of study and, in addition, although the student had already completed a degree, they were granted an additional remission on a second program that was less than 80 weeks in length without referral to the Appeals Board;
  - for 2 students a remission was refused because they had exceeded the time permitted to complete their program of study. Our review indicated that the students had completed the program of study within the required time period and should have been granted a loan remission in connection with the loans negotiated under this program;

### 3.15 Loan Remission Program

- for 1 student a loan remission of \$5,225 was granted although they had exceeded the time permitted to complete their program of study. In this case, the student took 256 weeks to complete a program which required completion within 208 weeks (i.e. 176 weeks + 1 grace period of 32 weeks);
- for 1 student there was no evidence in the file that the student had completed their program of study; and
- for 1 student, a program of study which was not 80 weeks in length was determined to be acceptable without referral to the Appeals Board.

#### Recommendations

*The Department should ensure that students are clearly notified of the existence and nature of the Loan Remission Program at the time of their first loan application so that students have an opportunity to plan for the completion of their studies in a fashion that will permit them to qualify for a loan remission upon completion of their studies.*

*Loan Remissions should be processed and forwarded to CIBC prior to the deadline established for the waiving of risk premium charges.*

*Loan Remission applications should be processed in accordance with Loan Remission Guidelines.*

#### Department's Response

*While all the specific details related to the Loan Remission Program were not finalized in 1994, the key parameters of timely completion and debt threshold were. These two key criteria were highlighted in materials released to the public in 1994.*

*General information related to the Loan Remission Program has been included in the General Information and Loan Application Guide since the 1995-96 loan year. A detailed program description has been included since 1997-98, the first year students were eligible to apply.*

*The Department of Education was more flexible with respect to the 90 days requirement early in the administration of the program in an effort to give students every opportunity to avail of the program. However, since 1998 the Department has been rigorously enforcing the 90 day criteria.*

### **3.15 Loan Remission Program**

*With the enforcement of the 90 day criteria, loan remissions are forwarded to CIBC prior to the deadline for avoiding risk premium charges.*

*The Department will be taking additional steps to ensure that loans remissions applications are processed in accordance with the Loans Remission Guidelines.*

### 3.16 Student Loan Program

#### Introduction

In 1994-95, the Department of Education and Training commenced the delivery of the Newfoundland Student Loan program through its Student Aid Division. The Newfoundland Student Loan Program is delivered along with the Canada Student Loan Program. While both loan programs are separate from one another, there is sufficient harmony in the loan programs to permit delivery as one program. Student loans are issued at 60% and 40% under the federal and provincial programs respectively and the costs of servicing are shared, for the most part, on the same basis.

Currently, there is no written agreement between the Federal government and the Province governing the delivery of the Canada and Newfoundland Student Loan Program by the Province; however, the Province does receive an annual fee from the federal government equal to approximately 50% of the administrative costs it incurs to deliver both loan programs. A harmonized loan agreement is expected to be signed in the near future that will govern the administration of a new harmonized loan product that is expected by August 2000.

Student loans are based on specific eligibility criteria and assessed need and they are intended to supplement the resources of students and their families. The maximum combined amount a student can borrow under the Canada and Newfoundland Student Loan Program is limited to \$275 per week of study (\$165 Federal and \$110 Provincial) to a lifetime maximum of 340 weeks for students who commenced borrowing on or after 1 August 1995. Prior to this, the maximum number of weeks of borrowing was 520.

On 1 September 1994, the Province entered into an exclusive five year agreement with the Canadian Imperial Bank of Commerce in which the bank agreed to make loans to students and assume the risk of loan default in return for a five percent risk premium calculated on outstanding principal loan balances at the time student loans go into repayment. Students deemed eligible for a student loan by the Department must negotiate and repay their Newfoundland Student Loans with the Canadian Imperial Bank of Commerce in accordance with the terms of an agreement between the Province and the Canadian Imperial Bank of Commerce. Canada Student Loans can be negotiated and repaid through a variety of financial institutions. The interest portion of the students loan is paid by both governments while the student is in school. After the student completes his/her period of study, interest begins to accrue to the student who must consolidate all outstanding student loans and commence repayment within six months.

Figure 1 shows the total number, total dollar value and average dollar value of loans made for the past 5 years.

### 3.16 Student Loan Program

Figure 1

**5 Year Summary of Financial Assistance  
Approved for Full Time Study  
Academic Years ended 31 July**

| Year    | Number of Students | Canada Student Loans Approved (\$ Millions) | Newfoundland Student Loans Approved (\$ Millions) | Total Student Loans Approved (\$ Millions) | Average Student Loan Approved (\$ Thousands) |
|---------|--------------------|---------------------------------------------|---------------------------------------------------|--------------------------------------------|----------------------------------------------|
| 1994/95 | 14,256             | \$57.1                                      | \$32.3                                            | \$89.4                                     | \$6.3                                        |
| 1995/96 | 16,534             | \$76.4                                      | \$46.1                                            | \$122.5                                    | \$7.4                                        |
| 1996/97 | 21,226             | \$103.8                                     | \$66.2                                            | \$170.0                                    | \$8.0                                        |
| 1997/98 | 21,922             | \$104.7                                     | \$68.1                                            | \$172.8                                    | \$7.9                                        |
| 1998/99 | 21,312             | \$106.8                                     | \$70.8                                            | \$177.6                                    | \$8.3                                        |

Source: Student Aid Management Information System

As Figure 1 indicates, the number of students approved for loans in 1998-99 has increased by 50% since 1994-95, mainly due to an increase in the number of students attending private colleges. While the average student loan approved during that period has increased by 32%, the maximum loan available to the student has essentially remained constant at \$275 per week during the five year period.

The Province's cost for the Newfoundland Student Loan Program consists of the following:

- interest on Newfoundland student loans while students are studying;
- a risk premium of 5% of the principal balance at the time the student is required to commence repayment;
- interest relief may be paid by the Province upon application by a student who can demonstrate that financial hardship would be incurred in repaying their loan;



### 3.16 Student Loan Program

- a loan becomes guaranteed and payable by the Province if at any time prior to loan consolidation the borrower is a minor, has become disabled, is deceased, or enters into an event of insolvency; and
- a loan becomes limitedly guaranteed and payable by the Province if a borrower with a history of credit abuse defaults on their student loan.

Figure 2 shows the costs which have been incurred by the Province over the past 5 years as a result of making Newfoundland Student Loans.

As Figure 2 indicates, the total costs have increased significantly since 1994-95 due to the significant increase in the number of students approved for loans during the time period and the cumulative effect of the same students approved for loans year after year until graduation occurs. Since 1994-95, costs directly related to the Newfoundland Student Loan Program have increased by \$11 million. Increases in interest subsidy costs account for 56% of the \$11 million increase in costs.

As of 31 March 1999 there was \$223 million in issued and outstanding student loans of which \$87 million relates to loans currently on repayment by students who have completed their studies. Of the \$87 million in student loans which is currently subject to repayment, \$29.4 million or 34% is in arrears greater than 30 days. This is similar to 31 March 1998 when \$18.5 million or 35 % of the \$50.3 million in student loans under repayment were in arrears greater than 30 days.

**Figure 2**

**Costs Incurred in Relation to  
Full Time Student Loans Approved  
Years ended 31 March  
(\$ Millions)**

|                | <b>Interest<br/>Subsidy</b> | <b>Risk<br/>Premium</b> | <b>Interest<br/>Relief</b> | <b>Guaranteed<br/>Loans</b> | <b>Administrative<br/>Costs*</b> | <b>Total</b> |
|----------------|-----------------------------|-------------------------|----------------------------|-----------------------------|----------------------------------|--------------|
| <b>1994/95</b> | \$ .4                       | \$ .0                   | \$ .0                      | \$ .0                       | \$ .8                            | \$1.2        |
| <b>1995/96</b> | \$2.2                       | \$ .8                   | \$ .0                      | \$ .0                       | \$ .8                            | \$3.8        |
| <b>1996/97</b> | \$2.7                       | \$1.2                   | \$ .2                      | \$ .0                       | \$1.0                            | \$5.1        |
| <b>1997/98</b> | \$4.1                       | \$1.5                   | \$ .5                      | \$ .7                       | \$1.3                            | \$8.1        |
| <b>1998/99</b> | \$6.6                       | \$2.1                   | \$1.1                      | \$1.2                       | \$1.3                            | \$12.3       |

Source: Student Aid Annual Report, \* Public Accounts



### 3.16 Student Loan Program

- a loan becomes guaranteed and payable by the Province if at any time prior to loan consolidation the borrower is a minor, has become disabled, is deceased, or enters into an event of insolvency; and
- a loan becomes limitedly guaranteed and payable by the Province if a borrower with a history of credit abuse defaults on their student loan.

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|----------------|-----------------------------|-------------------------|----------------------------|-----------------------------|----------------------------------|--------------|
| <b>1994/95</b> | \$ .4                       | \$ .0                   | \$ .0                      | \$ .0                       | \$ .8                            | \$1.2        |
| <b>1995/96</b> | \$2.2                       | \$ .8                   | \$ .0                      | \$ .0                       | \$ .8                            | \$3.8        |
| <b>1996/97</b> | \$2.7                       | \$1.2                   | \$ .2                      | \$ .0                       | \$1.0                            | \$5.1        |
| <b>1997/98</b> | \$4.1                       | \$1.5                   | \$ .5                      | \$ .7                       | \$1.3                            | \$8.1        |
| <b>1998/99</b> | \$6.6                       | \$2.1                   | \$1.1                      | \$1.2                       | \$1.3                            | \$12.3       |

Source: Student Aid Annual Report, \* Public Accounts

### 3.16 Student Loan Program

#### Scope and Objectives

We completed our review of the Newfoundland Student Loan Program in April 1999. Our review included a review of student loans made during the academic year 1997-98 and the academic year 1998-99 up to 31 March 1999. Our objectives were to determine:

- whether the Department has established administrative policies and procedures regarding the Newfoundland Student Loan Program and that there was compliance with the policies and procedures; and
- whether the Department has established performance indicators and monitoring procedures for use in evaluating its delivery of the Newfoundland Student Loan Program, and whether there is adequate and appropriate reporting of program activity to ensure discharge of accountability.

#### Conclusions

Currently, there is no written agreement between the Federal government and the Province governing the delivery of the Canada and Newfoundland Student Loan Program by the Province.

The current *Student Assistance Act* was enacted in 1996 and does not adequately reflect the changes which occurred in 1994-95 when the Province moved from a grants based program to a loans based program. In addition, in 1996 the *Student Allowances Regulations*, which related to student programs that are no longer available, were eliminated. As a result, the Newfoundland Students Loan Program is currently being administered without the appropriate legislative authority.

The Department does not have its own policy manual for the administration and delivery of its student loan program. The Department maintains that it is administering its student loan program, for the most part, in accordance with policies issued by the Federal government for its Canada Student Loan Program. However, our review indicated many instances of non-compliance with these policies as follows:

- The Department did not monitor and limit loan eligibility with respect to students who did not complete their program of study within time frames outlined in the policies prior to the 1998-99 academic year. The Department's failure to monitor this also impacts on students wishing to qualify for a loan remission at graduation, since timely completion is one of the criteria which must be met.

### 3.16 Student Loan Program

- While the policy states that tuition and compulsory fees should be assessed at the actual amounts payable to the educational institution, information to support this is not always on file.
- The Department is determining the student's pre-study financial contribution solely based on 80% of the students discretionary income for that period and has not been factoring the required established minimum student contribution into the determination of the students pre-study contribution. As a result, some students are receiving loans in excess of entitlement.
- Pre-study income information provided by students is not always verified, income confirmation forms are not always subsequently provided by students and there were instances where student contributions were calculated incorrectly.
- Income reported by students in their 1998-99 loan applications was not verified. The Department has identified approximately \$190,000 in over-awards as a result of auditing 10% of student borrowers from the 1997-98 academic year. When this error rate is projected over all student loans approved that year, over-awards could total approximately \$2 million, 40% of which relates to the Province's portion of the student loan.

The appeals process is currently coordinated through an Appeals Officer and an Appeals Board. There are weaknesses in the student loan appeals process as follows:

- Although there is no legislative authority for the Appeals Board, it is apparent that the Department continues to support the Appeals Board as it continues to exist. While we support the existence of an appeals board, its independence would be enhanced if all members were independent of Government.
- We found it difficult to determine the conditions that must exist before an appeal will be heard by the Appeals Board and there is no evidence that students are advised that an Appeals Board exists.
- The Department could not determine the number and nature of student appeals received in the past year, how many were approved and rejected, and how fast the appeals were being processed. As of 23 April 1999 there were 149 appeals awaiting processing by the Appeals Officer from 23 March 1999 and earlier.

### 3.16 Student Loan Program

In order for students to be eligible for student loans, the institution they are attending must be "designated" for purposes of student loans under the *Student Assistance Act*. The *Student Assistance Act* does not provide any guidance as to how an educational institution should be designated for purposes of student loans since there are no regulations established for this purpose under the *Act*, even though there is provision in the *Act* to do so. The Department maintains that it has been designating private educational institutions for purposes of student loans if they meet private training institution licencing requirements under the *Private Training Institutions Act*. Effective 1 January 1999, for purposes of student loans, the Private Training Institutions Regulations were amended to state that "*Notwithstanding the Student Assistance Act or regulations, a private training institution shall not be designated as an institution which offers courses for which student assistance is available unless it has been in continuous operation as a registered private training institution for one year and has graduated one class of students*".

There are no approved guidelines or procedures in place to ensure that the Department can effectively monitor student loan default rates at designated educational institutions. Designated educational institutions with unacceptable student loan default rates may indicate that these institutions are experiencing program and/or operational problems. Our review indicated that for 1997-98, 23 of 54 educational institutions in this province had student loan default rates in excess of 30%. We could not determine if these default rates were acceptable to the Department. Draft Canada Student Loan Designation Guidelines as prepared by the Federal Government for discussion purposes, for example, suggest that for 1997-98, institutions with default rates greater than 30% and less than 55% should be placed on "probation".

In October 1998, an internal departmental committee released its report on "Designation for Student Aid Purposes" to address weaknesses in the Provincial designation process. The Department has indicated that it intends to forward its draft designation policy to educational institutions for their input in the near future. We are concerned that a report dated October 1998 on such a significant issue has yet to be implemented in light of the significant increase in the number of students attending private educational institutions.

The Department has not reviewed error reports related to billings from the bank for interest subsidy, interest relief and risk premiums since December 1996. Our review of the exception report dated 31 October 1998 indicated that the exceptions total approximately \$840,000. These exceptions could represent amounts paid by the Department in error.

### 3.16 Student Loan Program

The Department has honoured guarantees on defaulted loans totalling \$1.9 million. It is now the Department's responsibility, and not the bank's, to collect these loans. The Department does not have any policies on the collection of these loans. Although some former students offered to repay their loans, the Department would not accept payments because it did not have a collection process in place.

The Province is currently negotiating an extension to the lender agreement in place with the bank with respect to student loans that expired on 31 July 1999. As a result of increasing student loan default rates and the Department's failure to adequately monitor student loan default rates, the Province is expecting the 5% risk premium it is currently paying on Class B student loans to increase to between 10% and 15%. This will result in risk premium costs increasing from \$2.1 million in 1998-99 to between \$4.7 million and \$6.6 million in 1999-2000.

The automated system being used to handle student telephone inquiries is not adequate. Information obtained from the Department indicated that there is an average of 2,290 calls per day made to this system and the majority of callers do not utilize its automated features, but request to speak to the operator instead. One operator cannot process all these inquiries in a timely manner.

The Switchboard at Student Aid is intended to direct callers to their appropriate destination. We found that a significant percentage of calls made to the Student Aid switchboard operator are abandoned before the switchboard operator can answer.

The Department has not established goals, objectives and performance indicators for the Newfoundland Student Loan Program. While the Student Aid Annual Report is a comprehensive and detailed document, the information provided in it cannot be utilized in monitoring performance because the Department has not established goals and objectives to compare the information against. In addition, the Department is not compiling performance information such as the length of time it takes to process an application for a student loan or the length of time it takes to process appeals.



### 3.16 Student Loan Program

#### Findings and Recommendations

##### 1. Legislative Authority for the Student Loan Program

The *Student Assistance Act* provides for the payment of financial assistance to students attending post-secondary educational institutions. The current *Act* was enacted in 1996 and does not adequately reflect the changes which occurred in 1994 when the Province moved from a grants based program to a loans based program. In 1996, an amendment was made to the *Act* to eliminate the *Student Allowances Regulations* which related to student programs that were no longer administered by the Province as a result of the implementation of the Newfoundland Student Loans program in 1994-95. However, new regulations relating to the new programs were never made. As a result, the Newfoundland Students Loan Program is currently being administered without the appropriate legislative authority.

##### 2. Departmental Policies

The Province does not have its own policy manual for the Newfoundland Student Loan Program. Since there is a high degree of harmony between the Newfoundland Student Loan Program and the Canada Student Loan Program, the Province maintains that it has been delivering its loan program, for the most part, in accordance with Canada Student Loan policy. Provincial exceptions to the Canada Student Loan policy are provided in the "General Information and Application Guide". With respect to Canada Student Loans, the Province is responsible for determining and monitoring the eligibility of students in accordance with Canada Student Loan policy.

The Canada Student Loan policy outlines the following:

- the **eligibility criteria** a student must meet to qualify for a student loan;
- the process which must be followed to conduct a **need assessment** for the student loan;
- the **appeals** process; and
- the procedures for the **designation of educational institutions** for purposes of student loans.

### **3.16 Student Loan Program**

Our review of the above four policies indicated the following:

**(a) Eligibility Criteria**

In order to be eligible to receive a student loan from the Department the student is required to be a resident of this province, be enrolled full time in a designated educational institution, maintain a satisfactory scholastic standard, and complete his/her program study within the required time period. We selected a random sample of student loans in the 1997-98 and 1998-99 academic years. Our review indicated the following:

**(i) Province of Residence**

Canada Student Loan policy requires that students must apply for student loans in the Province they are considered to reside. Our review of the samples selected did not identify any exceptions in this area.

**(ii) Maintenance of Scholastic Standards**

Canada Student Loan policy requires that a student maintain a satisfactory scholastic standard to continue to be eligible for Canada Student Loans. Satisfactory scholastic standard is successful completion of at least 60% of a full course load at the post-secondary level. Currently, in accordance with the "Post Secondary Institutional Guide to Newfoundland Student Financial Assistance", educational institutions are required to advise the Department when a student has withdrawn from a program of study or has been terminated by the educational institution for poor academic achievement. A student's failure to maintain scholastic standards for one period of study requires that they be placed on probation, two periods of study requires that they lose loan eligibility for 12 months, and three periods of study requires that they lose loan eligibility for 36 months.

Our review indicated that the Department is not monitoring a student's scholastic standard in accordance with Canada Student Loan policy because there is no monitoring of educational institutions to ensure that they are providing the Department with the required student withdrawal and termination information in a complete and timely manner. As a result, Student Aid may be providing loans to students who are not maintaining satisfactory scholastic standards.



### 3.16 Student Loan Program

#### (iii) Duration of Assistance

- Canada Student Loan policy requires that the maximum duration of eligibility for student loans be based on the student's program period of study plus a grace period of one. For example, a student studying a 4 year (128 weeks) program at Memorial University of Newfoundland would be eligible for 5 years (160 weeks) of student loans. A student may complete more than one program or transfer programs and remain eligible for student loans up to a lifetime limit of 340 weeks if borrowing commenced after 1 August 1995 or 520 weeks if borrowing commenced before 1 August 1995. Canada Student Loan policy permits the Province to limit the number of programs a student may borrow under.

Our review indicated that the Department was not monitoring duration of assistance prior to the 1998-99 academic year and was not monitoring or limiting program transfers prior to the 1997-98 academic year. Current monitoring is also based on the number of borrowing weeks a student has in a program and not the number of actual weeks the student has in a program which could potentially allow a student to exceed the Canada Student Loan program plus one limit.

Our review indicated that in 4 of 24 loan applications the student had transferred programs and/or institutions at least three times, did not earn a degree and had compiled significant debt. In one case, a student transferred programs five times and had borrowed for 347 weeks for a total of \$58,828. The student requires an additional 32 weeks of borrowing to earn a degree and this has been approved by the Department. On graduation, this particular student will have borrowed for 379 weeks of study and compiled a debt in excess of \$65,000 for a program of study that normally requires 128 weeks of study to complete.

### **3.16 Student Loan Program**

Although, Canada Student Loan policy states that the limiting of program transfers is a Provincial issue, the Province did not establish a program transfer policy until 1997-98. In our opinion, the Department's failure to establish a program transfer policy and monitor student duration of assistance may have contributed to the increasing debt load of students in some cases.

- Canada Student Loan policy specifies that students are not eligible for loans to repeat a period of studies previously completed solely to improve grades. Discussion with officials at the Department indicated that there is no system in place to monitor this. Further discussion revealed that the Department is not advising students that they cannot apply for a loan to repeat courses to improve grades. As a result, Student Aid may be providing loans to students who do not qualify due to their repeating of courses to improve grades.

#### **(b) Need Assessment**

The need assessment process includes the identification of a student's category (e.g. single dependent, single independent, married, and single parent), an assessment of the student's cost of post-secondary study, an assessment of the resources available to the student and a calculation of the student's need. Students are eligible for loans up to the amount of their need provided this does not exceed the maximum student loan that is available for the period. Our review indicated the following:

##### **(i) Identification of Student Category**

Canada Student Loan policy requires that students be placed in predefined categories which reflect the students' living situation. This is necessary since students are assessed standard living costs for purposes of need assessment. Our review indicated that for all 24 loan applications, students appeared to be placed into categories that reflected their living situation in accordance with Canada Student Loan policy.

### 3.16 Student Loan Program

#### (ii) Assessment of Student Costs

Canada Student Loan policy requires that a student be assessed both education and living costs for the entire study period for purposes of need assessment. Our review indicated the following:

- Canada Student Loan policy states that tuition and compulsory fees should be assessed "*at the actual amounts payable to the educational institution*". This information is usually included on the "Course of Study and Educational Cost" form submitted to Student Aid by the student after it has been verified by the educational institution. Our review indicated that in 5 of 24 loan applications, there was no form on file to substantiate that the amounts assessed for tuition and compulsory fees were the actual amounts payable to the institution.
- Canada Student Loan policy states that the Province may establish average amounts for books and supplies subject to the maximum amount per institution up to \$3,000 per academic year. The Department reviewed book costs and has been using an average of \$350 per semester for 1997-98 and \$500 per semester for 1998-99 for all students. We could not determine if the average costs being used by the Department for books and supplies adequately reflects the costs being incurred by students at the various institutions or that the average amounts established were ever approved by the Department.

#### (iii) Assessment of resources available to the Student

Resources considered to be available to a student for purposes of need assessment mainly come from the student's income during the pre-study and study period, as well as from student assets. If the student is categorized as dependent, then a contribution from parental income may be required as well. Our review indicated the following:

### 3.16 Student Loan Program

- Canada Student Loan policy states that, *"the contribution expected from the pre-study period (immediately preceding 16 weeks) is the greater of the established minimum student contribution for the students category (which was \$371 per month in 1998-99) ..., or 80% of the student's ...discretionary income (after income taxes and certain living allowances) from the pre-study period"*.

Our review indicated that Student Aid is determining the student's pre-study contribution solely based on 80% of the students discretionary income for that period and has not been factoring the required established minimum student contribution into their determination of the students pre study contribution.

Our review also indicated that 16 of 24 loan applications had pre-study income contributions that did not meet the minimum student contribution. This increased student loans for 13 of the 16 applicants by amounts ranging from \$17 to \$1,598 for the semester for which the students were not entitled.

- Canada Student Loan policy states that income earned by students during the pre-study and study period is to be utilized as a resource for purposes of need assessment. Since this income is not accurately determinable at the time of the initial loan application, the student is required to submit an "Income Confirmation Form" later in the semester restating and verifying pre-study earnings and updating expected study period earnings. The student's initial loan is then reassessed based on this information. Our review of 24 loan applications for the academic period 1997-98 and 1998-99 indicated the following:
  - in 5 of 24 loan applications, there was no evidence that the student subsequently provided an Income Confirmation Form;

### 3.16 Student Loan Program

- in 6 of the 19 loan applications where an Income Confirmation Form was provided, there was no evidence that the Department obtained proof of the reported pre-study income. Discussions with officials in the Department indicated that there are no follow up procedures regarding students who do not provide proof of their pre study income; and
- in 2 of the 13 cases where an Income Confirmation Form and proof of earnings were provided by the student, the Department incorrectly calculated the students contribution resulting in the students obtaining loans in excess of what they were eligible for. The two students received \$524 and \$623 respectively in excess of their entitlement.
- Prior to the 1998-99 academic year, the Department required that the student provide an assessed copy of his/her prior year's tax return with their loan application. The student's tax return was compared with pre-study and study period income reported by the student in his/her prior year's loan application(s). Any significant discrepancy between income reported by the student on their loan application and income reported by the student on their tax return was investigated. Any resulting over-awards were recovered from the student's current and future loans.

In addition, Canada Student Loan policy states that parental contributions towards the education of dependent students is to be calculated based on the *"net income for the full taxation year prior to the students study period"* as reported on that year's income tax return. The Department dropped its requirement that students provide an assessed copy of their prior year's tax return with his/her loan application and that dependent students provide an assessed copy of their parents' prior year's tax return with his/her loan application(s) for the 1998-99 academic year. Discussion with officials at the Department indicated that this was done in

### 3.16 Student Loan Program

anticipation of utilizing an electronic verification system in conjunction with Revenue Canada where student and parental tax returns could be verified quickly and accurately by the system.

The Department's decision to drop its requirement that students provide an assessed copy of his/hers tax return and his/her parents tax returns was premature in that it has not signed an agreement with Revenue Canada that would enable this electronic verification system to become operational. As a result, the Department has not been able to verify student and parental income information reported by students on their loan application during the 1997/98 and 1998/99 academic years.

The Department maintains that it has identified \$190,716 in over-awards as a result of auditing 10% of student borrowers from the 1997-98 academic year. When this error rate is projected over all student loans approved that year, over-awards could total approximately \$2 million, 40% of which relates to the Province's portion of the student loan.

These over-awards will also increase the Province's interest subsidy and the risk premium or loan guarantee if the over-award is not recovered.

- Canada Student Loan policy states that, "*in addition to contributions from income, students are assessed a contribution based on the financial assets and vehicles registered in their name...or their spouse's name*". Our review indicated that Student Aid does not assess student contributions based on vehicles registered to students who apply for a loan. As a result, students who hold assets in the form of vehicles registered in their name or their spouses name, may receive higher student loans than the amount to which they are entitled.



### 3.16 Student Loan Program

#### (iv) Assessment of Student Need

Students are eligible for a loan when their assessed costs exceed their assessed resources. The student is eligible to receive a Canada Student Loan (60%) and a Newfoundland Student Loan (40%) up to the amount of their assessed need to a maximum of \$275 per study period week. Previous loans issued to students in excess of the eligible amount are called over-awards and are deducted from current student loans. Our review indicated the following:

- In accordance with provincial policy, there is no provision under the social assistance program to provide social assistance for single students or couples with no dependent children while they attend a post secondary educational institution on a full time basis. However, social assistance recipients with dependent children who attend a post secondary institution are required to borrow the maximum amount of student aid available to them during that time period, but, will have their social assistance benefits reduced by an amount agreed upon as "shelter" costs for the time period they attend school (the shelter component of their social assistance is recovered from the students loan since this is non allowable income in terms of determining social assistance benefits).

Discussion with officials at Student Aid indicated that social assistance recipients who do not qualify for maximum loans because their assessed need is not great enough, will have their education costs increased by whatever amount is necessary to equate the overall assessed need with maximum loans available. In effect, Student Aid are granting maximum student loans to all social assistance recipients whether they qualify for them or not.

- Canada Student Loan policy states that "*over-awards are deducted from the award eligible to be met by federal and provincial programs*". Our review indicated that in 1 of 4 cases where a student loan was processed when the student had an outstanding over-award on their file, the entire amount of the over-award was not collected from the students loan. Discussion with officials at the

### 3.16 Student Loan Program

Department indicated that the collection of over-awards will be deferred in cases where the student can demonstrate financial hardship. Canada Student Loan policy does not address the deferral in collection of over-awards and the Department has no policy in this area; and

- As at 21 April 1999, the Department determined that there were 8,700 students with outstanding over-awards on their file totalling \$8.4 million. Of these amounts, there were 4,300 students with over-awards totalling \$4.1 million who have not applied for a student loan since the 1996-97 academic year. Of the \$4.1 million, \$5 million related to Newfoundland Student Loans.

While the \$8.4 million represents loans which will at some point in time be payable to a bank by students, there is a cost which is borne by the Province. The Province is responsible for paying the risk premium, interest subsidy, and interest relief on the Provincial portion totalling \$1.6 million. In addition, for those loans guaranteed by the Province, the Province may be called upon to honour those guarantees.

#### (c) Appeals

Canada Student Loan policy states that a review of a student's loan assessment should be undertaken by the Province when the information provided by the student in support of the loan application has changed, when a student believes an error was made in the application of one of the loan criteria, and when there are extenuating circumstances which were not addressed in the need assessment procedures. Appeal Boards are required to adhere to principles outlined in the Canada Student Loan review criteria.

The Department has designated an Appeals Officer to review appeals submitted by students with respect to their loan assessment. The Department also has an Appeals Board in place to hear appeals from students who wish to pursue their appeal beyond the Appeals Officer, or in cases where a precedent has not been set. Our review of the appeals process and compliance with Canada Student Loan policy in this area, included an examination, on a random basis, of 16 student appeals between 1 January 1998 to 31 March 1999. Our review indicated the following:

### 3.16 Student Loan Program

- The Department does not monitor and is unable to provide information on student loan appeals including the number and nature of appeals received each year, how fast they are processed and how many are approved or rejected;
- As at 23 April 1999 there were 149 appeals dated 23 March 1999 and earlier awaiting review by the Appeals Officer. On average, we determined that it took 68 days for the Appeals Board to hear the 3 appeals received in the 1998-99 academic year and 48 days to hear the 11 appeals received in the 1997-98 academic year. We could not determine if this was satisfactory since there have been no targets established by the Department in this area;
- The Appeals Officer (not the Appeals Board) recently commenced hearing appeals with respect to students denied loans as a result of excessive program or institution transfers and/or failure to complete their program of study within the required time period. Our review indicated that the Department has not established any guidelines with respect to when a student should be permitted to continue his/her studies under these circumstances;
- The Appeals Board was established under the *Student Allowances Regulations* which no longer exist. As a result, the Appeals Board currently has no legislative authority under which it can operate. The *Student Allowances Act* provides legislative authority to make regulations establishing Boards and Committees; however, no regulations have been established to date;
- Although there is no legislative authority for the Appeals Board, it is apparent that the Department continues to support an Appeals Board as it continues to exist. The composition of the current Board complies with the old *Regulations* which no longer exist. The current five member Board includes two government employees. While we support the existence of an appeals board, its independence would be enhanced if all members were independent of Government;

### 3.16 Student Loan Program

- We found it difficult to determine the conditions that must exist before an appeal will be heard by the Board and there is no evidence that students are advised that an Appeals Board even exists. There is no reference to the students right to appear before the Board in the Student Application and Information Guide or in the Appeal Send Back Letter that the student receives after the initial decision is made by the Appeals Officer; and
- The Appeals Board has been relatively inactive since the 1996-97 academic year. Our review of Board minutes indicated that the Board heard 29 appeals in 5 meetings since the 1996-97 academic year. These meetings were held 25 September 1996, 12 February 1997, 16 May 1997, 20 November 1997, and 20 November 1998. In our opinion, the relative inactivity of the Board over the past three years may be attributable to the Departments failure to advise the student of their right to make an appeal to the Board.

#### (d) Designation of Educational Institutions

For students of educational institutions to be eligible for student loans, the institution must be "designated" for purposes of student loans. Our review of the current process used to "designate" educational institutions for student loans indicated the following:

- The *Student Assistance Act* does not provide any guidance as to how an educational institution should be designated for purposes of student loans since there are no regulations established for this purpose under the *Act*, even though there is provision in the *Act* to do so. The Department maintains that it has been designating private educational institutions for purposes of student loans if they meet private training institution licencing requirements under the *Private Training Institutions Act*. Under the *Private Training Institutions Act*, private training institutions must meet certain criteria in order to be licenced and remain licenced under the *Act*. These criteria include, among other things, providing education programs approved by the Department of Education, maintaining a security bond at an acceptable level, contributing to a "train out fund" and providing annual audited financial statements to the Department. Effective 1 January 1999, for purposes of student loans, the Private Training Institutions Regulations were amended to state that "Notwithstanding the Student

### 3.16 Student Loan Program

*Assistance Act or regulations, a private training institution shall not be designated as an institution which offers courses for which student assistance is available unless it has been in continuous operation as a registered private training institution for one year and has graduated one class of students".*

For a two year period prior to 1 January 1999, there was no requirement that private training institutions licenced under the *Private Training Institutions Act* be in continuous operation for any period of time for purposes of student loans.

- There are no approved guidelines or procedures in place to ensure that the Department can effectively monitor student loan default rates at designated educational institutions. The monitoring of student loan default rates is necessary to determine which institutions may be experiencing program and/or operational problems and may require Departmental supervision to rectify these problems.

Loan default rates for Newfoundland Student Loans are provided to the Department by the Canadian Imperial Bank of Commerce on a monthly basis. Default according to the Canadian Imperial Bank of Commerce is 61 days past due on Class B loans. Our review of the 1997-98 Student Aid Annual Report indicated the following default rates for Class B Newfoundland Student Loans:

- 2 of 8 Memorial University of Newfoundland campuses had default rates greater than 30%;
- 7 of 19 Public Colleges had default rates greater than 30%. One had a default rate of 46%;
- 14 of 27 Private Colleges had default rates greater than 30%. Three had default rates greater than 40%; and
- 1 of 43 institutions outside the province which were attended by students from Newfoundland had a default rate greater than 30%.

This information shows that for 1997-98, 23 of 54 educational institutions in this province had student loan default rates in excess of 30%.

### 3.16 Student Loan Program

Since the Department has not established acceptable student loan default rates for educational institutions, we could not determine if any of the default rates are acceptable to the Department or which institutions might require supervision to rectify unacceptable default rates. Draft Canada Student Loan Designation Guidelines as prepared by the Federal Government for discussion purposes, for example, suggest that for 1997-98, institutions with default rates greater than 30% and less than 55% should be placed on "probation".

Educational institutions with unacceptable student loan default rates may be an indication that the institution is experiencing program and/or operational problems which increases the risk that students will not receive a quality education at that institution, which could jeopardize the students opportunity for meaningful employment. A student unable to complete his/her education or unable to obtain meaningful employment on graduation may experience difficulty in repaying their student loan. This would affect loan default rates which are currently being reviewed by lenders to determine the adequacy of risk premiums currently being paid by the province on Class B student loans.

In October 1998, an internal departmental committee released its report on "Designation for Student Aid Purposes" to address weaknesses in the Provincial designation process. Specific recommendations were made to formally establish a designation, monitoring and de-designation policy for the province and a new draft policy was prepared. The committee report indicated that the province is concerned with increasing default rates and the number of private colleges experiencing operational problems. The Department has indicated that it intends to forward its draft designation policy to educational institutions for their input in the near future. Any new recommendations should strengthen probation procedures. Also, we are concerned that a report dated October 1998 on such a significant issue has yet to be acted upon, in light of the significant increase in the number of students attending private educational institutions.



### **3.16 Student Loan Program**

#### **(e) Loan Application Processing**

Efficient loan application processing is necessary to ensure that students receive financial assistance in a timely manner. Our review of the loan application process at the Department included an examination, on a random basis, of 50 loan applications processed for the 1997-98 academic year and 50 loan applications processed for the 1998-99 academic year. Our review indicated that the average time taken by the Department to process a loan application decreased from 36 days in 1997-98 to 17 days in 1998-99. Although the Department streamlined procedures, a significant factor in the improvement in time taken to process loan applications can be attributed to the Department's decision to discontinue manually verifying student and parental income information reported on the loan application, as discussed earlier in this report.

#### **3. Lender Agreement with Bank**

In September 1994, the Province entered into an exclusive 5 year agreement with the Canadian Imperial Bank of Commerce where the bank would make loans to eligible students under the Newfoundland Student Loans Program and the Province would provide certain credit support in connection with those loans. This agreement expired 31 July 1999 and was in effect during our audit. Officials are currently in negotiations with the bank for a new agreement. The agreement specifies the terms and conditions under which the province agreed to pay the bank interest on Class A loans (interest subsidy), interest relief on Class B loans, risk premiums on Class B loans, loan guarantees and limited loan guarantees.

#### **(a) Interest Subsidy, Interest Relief and Risk Premium Charges**

Each month, the bank invoices the Province for the interest subsidy, interest relief and risk premium costs. The bank provides an electronic tape with the monthly invoices which is verified with data contained in the Student Aid Information System. If the bank charges do not agree with the student information in the Student Aid Information System, an exception report is produced identifying possible errors.

### **3.16 Student Loan Program**

Our review of the 31 October 1998 invoice from the bank for approximately \$1.6 million indicated that the invoice was paid by the Department without reviewing the related exception report to determine the extent of possible invoice errors. In fact, the Department has not reviewed any exception reports since December 1996. Our review of the exception report dated 31 October 1998 indicated that the total exceptions approximate \$840,000 and could be the total paid in error by the Department.

#### **(b) Loan Guarantee and Limited Loan Guarantee Charges (Claims for Loss)**

In accordance with the agreement with the Canadian Imperial Bank of Commerce, the Province agreed to pay the bank the principal plus accrued interest on all loans it guaranteed. A loan becomes guaranteed and payable if at any time up to consolidation the borrower is a minor, has become disabled, is deceased, or enters into an event of insolvency. The Province also agreed to provide a limited loan guarantee on all Class B loans that have reached a delinquency status of 90 days or more with respect to students who were 22 years of age at the time of their first loan application and had a history of credit abuse.

The Province began paying bank claims for loss in May 1997 and has paid approximately 500 claims totalling approximately \$1.9 million as at 31 March 1999.

Discussions with officials at the Department indicated that there is currently no system in place to facilitate the collection of the approximately 500 loans totalling approximately \$1.9 million and that there have been no efforts made to collect any of these delinquent loans. Furthermore, it has come to our attention that there have been a number of students who have contacted the Department offering to repay these loans, but their offers to repay were not accepted by the Department because it did not have a collection process in place.

#### **(c) Expiration of Lender Agreement between the Province and the Bank**

The lender agreement between the Province and the Canadian Imperial Bank of Commerce expired on 31 July 1999. With the anticipated arrival of a new Federal-Provincial harmonized loan program in August 2000, the Province is seeking to extend its lender agreement with the bank for a one year period. This will enable the Province to negotiate a new agreement with lenders in accordance with the new harmonized loan program and in

### **3.16 Student Loan Program**

conjunction with new lender agreements which will be negotiated by the Federal government for its Canada Student Loans.

Our review of documents at the Department pertaining to lender agreement renewal with the bank indicate that an agreement extension of one year will likely cost the Province in terms of increased risk premium costs due to the bank's concerns about increasing borrower default rates and the Province's failure to monitor loan default rates at designated institutions, as was outlined earlier in this report. In accordance with the terms and conditions of the existing agreement with the bank, the Province pays a risk premium of 5% on all Newfoundland Student Loans that have reached the required loan consolidation date of six months following the students final period of study end date. The risk premium is a one time payment compensating the bank for assuming the risk of assuming the students loan receivable.

The Department is expecting that a one year lender agreement renewal with the Canadian Imperial Bank of Commerce will result in a risk premium rate of between 10% to 15%. As a result, the Department is expecting risk premium costs to increase from the \$2.1 million incurred in 1998-99 to between \$4.7 million and \$6.6 million in 1999-2000. The Province expects to negotiate a more favourable risk premium rate with lenders in a harmonized loan environment.

#### **4. Information Services to Clients**

Providing clients with prompt and efficient service is necessary in order to maintain client satisfaction with services provided. Officials at the Department of Education indicated that there have been a number of students contacting the department to register complaints about the inadequacy of the telephone system at the Student Aid Office. Specifically, they cannot get through to an operator within a reasonable period of time in order to have their inquiries addressed. Throughout the course of our review, numerous letters and e-mail inquiries were observed in student files that supported this. The Student Aid office has two telephone systems in place. The first is a switchboard system and the second is an Interactive Voice Response System.

##### **(a) Switchboard (729-5849)**

The Switchboard is intended to direct inquiries from students and other sources to the appropriate destination during the business hours of 9:00 AM to 4:30 PM. As a result, calls taken by the switchboard operator should be short in duration. For example,

### 3.16 Student Loan Program

should inquiries be received from a student, they are required to be immediately transferred to the Interactive Voice Response System. The switchboard also has a queuing system which holds up to 20 people in a holding pattern. Our review of switchboard activity for the period 9 September 1998 to 15 September 1998 and 4 January 1999 to 8 January 1999 indicated the following:

- an average of 273 calls per day were received in the September time period. An average of 83 calls per day (30%) were abandoned before the switchboard operator answered. The average time a caller spent waiting for the switchboard operator to answer before abandoning was 1.3 minutes, with a maximum time of 7.9 minutes being recorded. The maximum time a caller waited for the switchboard operator to answer their call was 10 minutes.
- an average of 333 calls per day were received in the January time period. An average of 146 calls per day (45%) were abandoned before the switchboard operator answered. The average time a caller spent waiting for the switchboard operator to answer before abandoning was 1.2 minutes, with a maximum time of 7.1 minutes being recorded. The maximum time a caller waited for the switchboard operator to answer their call was 9.7 minutes.

**(b) Interactive Voice Response System  
(729-4244, 1-888-657-0800)**

The Interactive Voice Response System was implemented in August 1995. The system is automated and provides the student with the ability to access Student Loan information without having to speak to anybody. In this regard, the system is not limited to office hours. There is also a toll free number for students calling from outside the St. John's area. The Interactive Voice Response System will provide the student with information regarding the status of their application, the dates their loan certificates were issued, as well as providing students with the option of leaving messages to have forms forwarded to them in the mail. Students also have the option of speaking to the Interactive Voice Response System representative during business hours. Our review of the Interactive Voice Response System activity for the six month period 01 August 1998 to 31 January 1999 indicated the following:

- there was an average of 66,688 calls to the Interactive Voice Response System per month, or, 2,290 calls per day for the six month period August 1998 to January 1999,

### 3.16 Student Loan Program

- 65% of the callers requested to speak to the Interactive Voice Response System operator on duty. This means that approximately 1,489 callers per day, or 213 callers per hour requested to speak to the Interactive Voice Response System operator to have their inquiries answered. Given the volume of calls being directed to the Interactive Voice Response System operator on a daily basis, it is not possible for a single person to address all of the calls in a timely manner, and
- 62% of the callers did not access automated student aid information available through the IVR system for reasons which were not determinable.

Discussions with officials at the Student Aid office indicated that they have been aware of the Interactive Voice Response System problems for the past two years and were in the process of redesigning the system to provide a more efficient service.

### 5. Performance Indicators, Monitoring and Reporting Procedures

Clearly stated operational goals and objectives are necessary to ensure the proper establishment of performance indicators, monitoring and reporting procedures. In this regard, the Department completed a Student Aid Divisional Planning Document in 1998 outlining the Divisional Mission and Mandate, its Goals and Objectives and certain Performance Indicators. Our review of this document indicated the following:

- there is no evidence that the stated mission, mandate, goals, objectives and performance indicators were ever approved by Department Executive;
- goals, objectives and performance indicators stated in the document mainly relate to the development of policy and procedures for the Student Aid Division. Clearly established goals, objectives and performance indicators do not exist for such things as loan default rates per educational institution, compliance with CSL policy, application processing speed, student inquiry processing speed, average student debt load, and duration of loan assistance; and
- there is no evidence that the performance indicators stated in the document are being regularly monitored and reported to ensure stated goals and objectives are being achieved.

### **3.16 Student Loan Program**

The Department does produce a rather comprehensive and informative annual report regarding the various programs it administers. However, the majority of information being reported cannot be utilized in monitoring performance since there are no stated goals and objectives to compare the information against.

#### **Recommendation**

*The Department should consider the issues raised in this report and take appropriate action.*

#### **Department's Response**

*The Department is currently conducting a detailed review of the Student Loan Program, addressing both structural and delivery issues. In addition, discussions are ongoing with the Federal Government to harmonize the Canada Student Loan Program and the Newfoundland Student Loan Program into one uniform, portable, "one student-one loan" product.*

##### **1. Legislative Authority**

*The Department of Education is presently preparing a draft Student Assistance Act, in order to establish a new legislative base for the program.*

*While there is no specific written agreement between the Federal Government and the Province governing the delivery of the Canada Student Loan Program, it is widely understood that the Canada Student Loans Act, CSL Regulations, and CSL Program Administrative Criteria, constitute the formal arrangements between the Learning and Literacy Directorate of the Department of Human Resources Development Canada and the provincial authorities, to ensure the Program is administered with uniformity, both in the assessment of students' need, and in administrative practices followed.*

##### **2. Departmental Policies**

*The Student Aid Division has a General Information and Application Guide which clearly defines the policies and procedures governing the administration of the student loan program. This guide is used in conjunction with the detailed Federal Student Loan Manual in the administration of the programs.*

*The Department currently monitors the "period of study plus one" policy which limits loan eligibility, thereby encouraging students to complete their program of studies on a timely basis.*



### 3.16 Student Loan Program

*While there may be isolated cases where information related to tuition and compulsory fee costs is not on file, applications from students will not be processed until the institution confirms this information.*

*It is true that the province has not been requiring a minimum pre-study income contribution. However, this is only in cases where a student has been unable to find employment. A similar practice is followed in other jurisdictions and the federal government has agreed to the continuance of the practice in a new harmonized environment. This issue is also being considered as part of the Department's current review.*

*Normally the only situations where pre-study income information would not be verified is where students are not returning for subsequent semester(s). The student aid computerized system is designed in such a way that loans for subsequent semesters will not issue if the pre-study income is not verified. For the most part calculations are done electronically; the only exception to this is a calculation for a MUN student who applies for assistance in the winter semester, having not received any assistance in the fall semester. This represents a very small proportion of the total number of applicants.*

*The Department recognizes the importance of verifying student and parental income information reported by applicants, and has implemented an electronic exchange of information arrangement with Revenue Canada to address this issue.*

*The structure and operations of the Appeals Board will be addressed in the new Student Assistance Act. The General Information and Application Guide outlines the Appeals process. The practice has been that only those situations which represent a set of circumstances not previously adjudicated by the Appeal Board are referred to the Board. However, all students have the option of appearing before the Board if they so desire. The Department keeps records of those students who bring their cases to the Appeals Board, and also recently implemented an electronic system that records the status of every appeal.*

*Federal legislation delegates the authority to designate education institutions to provinces/territories. The Designation Guidelines referred to in the report are simply draft suggestions provided to the provinces/territories by the federal government in 1995. There was no requirement for provinces/territories to adopt these draft guidelines. In the designation of institutions in this province, institutions are required to meet the criteria pertaining to financial viability articulated in the Private Training Institution legislation. The policy governing designation is also one of the areas currently being analyzed as part of the comprehensive review of student aid the department recently initiated.*

### **3.16 Student Loan Program**

*The Department is concerned about higher Risk Premiums, and notes that this national issue is highlighted in the Harmonization Agreement discussions and Lenders' Negotiations. Guiding Principles have been suggested by the federal government in order to facilitate a national approach to the designation and de-designation process of institutions.*

#### **3. Lender Agreement**

*While the Department does not have a formalized system in place relative to collection of amounts paid out under the Loan Guarantee component, payments have been accepted from students pertaining to claims the province has paid CIBC. The Department has also recruited a Collection Officer and a Clerk to formalize the collection process and review the CIBC Error Reports.*

#### **4. Information Services to Clients**

*The Department has implemented new features to improve the IVR service. Statistics for October show that out of the 16,404 calls made to the IVR system only 442 were transferred to an operator for further information (2.7%) while the percentage for the month of November reflect a 2.4% transfer ratio. This represents a major decline in the percentage of callers who require operator service and indicates that the improved IVR system is much more responsive to the needs of callers.*

#### **5. Performance indicators, Monitoring and Reporting Procedures**

*The issue of establishing goals, objectives, and performance indicators for the Newfoundland Student Loan Program will be considered within the context of Government's broader Business Planning and Accountability initiatives. However, the Department does currently produce a comprehensive annual report on Student Aid, and does monitor key indicators, in particular the amount of time required to process an application. Since applications are processed based on date received, starting with the earliest outstanding batch, the number of days required to process applications is readily determined based on a determination of the date of the batch currently in process. During peak periods, this information was conveyed by the Director to staff on a weekly basis. Given that the application receipt date and processing date are also coded on the application database, the Department will also be examining the possibility of producing summary statistics on a regular basis.*

### 3.17 Monitoring of School Boards

#### Introduction

In 1996 the school system in the Province was reorganized with the dissolution of 27 church run school boards and the creation of 10 new English language school boards and one French language school board. The 27 school boards continued to exist and administer the schools within their jurisdiction until their dissolution on 31 December 1996. As at 31 December 1996, there were approximately 445 schools in the Province with a total enrolment of 110,450 students. Figure 1 provides a profile of the 11 school boards for the 1998-99 school year. As the figure indicates, the number of schools and student enrolment have declined by 18% and 12% respectively, in the past three years.

Figure 1

#### Department of Education School District Profile 1998-99

|  | District                          | School District | Number of |          |
|------------------------------------------------------------------------------------|-----------------------------------|-----------------|-----------|----------|
|                                                                                    |                                   |                 | Schools   | Students |
| 1                                                                                  | Labrador                          |                 | 19        | 5,516    |
| 2                                                                                  | Northern Peninsula\Labrador South |                 | 33        | 3,769    |
| 3                                                                                  | Cornier Brook\Deer Lake\St. Barbe |                 | 31        | 8,610    |
| 4                                                                                  | Stephenville\Port aux Basques     |                 | 30        | 6,598    |
| 5                                                                                  | Baie Verte\Central\Connaigre      |                 | 48        | 9,494    |
| 6                                                                                  | Lewisporte\Gander                 |                 | 34        | 9,248    |
| 7                                                                                  | Burin Peninsula                   |                 | 21        | 4,913    |
| 8                                                                                  | Vista                             |                 | 18        | 4,868    |
| 9                                                                                  | Avalon West                       |                 | 45        | 11,461   |
| 10                                                                                 | Avalon East                       |                 | 80        | 32,656   |
| 11                                                                                 | Conseil scolaire francophone      |                 | 6         | 268      |
| Total                                                                              |                                   |                 | 365       | 97,401   |

Source: Department of Education's *Education Statistics 1998-99*

### **3.17 Monitoring of School Boards**

In the reorganization process, the Province decided to eliminate the existing debt of the 27 school boards as at 30 June 1996. As a result, in March of 1997, the Province paid the 10 district boards \$24.2 million to retire existing long-term debt and operating debt as of 30 June 1996. However, this did not completely eliminate the deficits as the boards operated from July to December 1996 and additional deficits arose. In March of 1999, the Province paid an additional \$1.2 million to five school boards to cover these additional operating deficits.

As part of the on-going audit work of our Office, we review the financial statements and other information of school boards annually. Our review of school boards in 1999 included an assessment and comparison of the financial position and operating results of each of the 11 boards.

#### **Financial Position**

Our review of school board financial statements, as summarized in Figure 4, disclosed that 7 of the 11 school boards had incurred bank indebtedness totalling \$4.3 million as at 30 June 1999 to finance board deficits and other expenditures. Six of these school boards had accumulated deficits of \$2.8 million for operations other than severance pay accruals. These deficits ranged from \$39,000 for District #2 to \$1.5 million for District #7. The remaining 5 boards had accumulated surpluses ranging from \$35,000 for District #4 to \$3.9 million for District #10. A summary of these surpluses and deficits is provided in Figure 2.

### 3.17 Monitoring of School Boards

Figure 2

**Department of Education  
School Boards  
Accumulated Surplus (Deficit)  
For the Years Ended 30 June  
(\$ 000's)**

| District     | 1999            |                 |              | 1998            |                 |              |
|--------------|-----------------|-----------------|--------------|-----------------|-----------------|--------------|
|              | Total           | Severance       | Operating    | Total           | Severance       | Operating    |
| 1            | (4,970)         | (4,671)         | (299)        | (4,914)         | (4,580)         | (334)        |
| 2            | (4,063)         | (4,024)         | (39)         | (3,540)         | (3,645)         | 105          |
| 3            | (9,334)         | (9,028)         | (306)        | (9,321)         | (8,978)         | (343)        |
| 4            | (7,156)         | (7,191)         | 35           | (7,185)         | (6,951)         | (234)        |
| 5            | (10,153)        | (10,798)        | 645          | (9,950)         | (10,579)        | 629          |
| 6            | (10,265)        | (9,813)         | (452)        | (10,072)        | (9,576)         | (496)        |
| 7            | (6,740)         | (5,232)         | (1,508)      | (6,301)         | (5,119)         | (1,182)      |
| 8            | (4,852)         | (4,688)         | (164)        | (4,019)         | (4,061)         | 42           |
| 9            | (10,188)        | (10,591)        | 403          | (9,918)         | (10,522)        | 604          |
| 10           | (22,808)        | (26,700)        | 3,892        | (22,981)        | (26,635)        | 3,654        |
| 11           | (82)            | (167)           | 85           | 120             | -               | 120          |
| <b>Total</b> | <b>(90,611)</b> | <b>(92,903)</b> | <b>2,292</b> | <b>(88,081)</b> | <b>(90,646)</b> | <b>2,565</b> |

Source: School boards' audited financial statements, except unaudited 1998-99 figures for District 7.

In summary, the 11 school boards had accumulated deficits totalling \$90.6 million for the year ended 31 March 1999. This is comprised of \$92.9 million in accrued severance pay, which the Department of Education does not fund, and a net accumulated operating surplus of \$2.3 million.

Our review of the financial position of the 11 school boards did not identify any significant problems with the exception of School Board #7, Burin Peninsula School Board, which had an accumulated operating deficit of \$1.5 million as at 30 June 1999 which is comprised of a \$700,000 deficit in 1996-97, a \$400,000 deficit in 1997-98 and a \$400,000 deficit in 1998-99. In addition, this Board was unable to provide us with audited financial statements for the year ended 30 June 1999 at the time of our review in November 1999.





### 3.17 Monitoring of School Boards

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### 3.17 Monitoring of School Boards

#### Compliance with Legislation

Subsection 65.(3) of the *Schools Act, 1997* states that:

*A board shall not in a fiscal year, contract for or become liable for an expenditure or debt that is more than the estimated expenditure or debt set out in its annual budget except with the prior written approval of the minister.*

During 1998-99, 5 of the 11 boards incurred operating deficits. There was no approval given by the Minister to these 5 boards. As a result, these boards did not comply with the *Schools Act, 1997*.

In addition, subsection 65.(1) of *Schools Act, 1997* requires each school board to submit its annual budget to the Minister at a date determined by the Minister. In correspondence dated 26 June 1998 the Department requested that each board submit its budget no later than 30 September 1998 for the 1998-99 fiscal year. Only 4 of the 11 boards submitted the required budget and none of these were received by the required date, 30 September 1998. Two budgets were received in October 1998, one was received in November 1998 and one was received in January 1999. As of the date of our review in November 1999, the Department had not received the 1998-99 budgets for the remaining seven school boards and had received the 1999-2000 budgets from only 3 of the 11 school boards.

#### Operating Results

Using 1995-96 as the base year which was the last full year that the former 27 school boards operated, school board provincial revenues have declined by \$27.0 million, including \$18.5 million in teaching services grants and \$8.5 million in other revenues. The total revenue per pupil increased by 7% from \$4,796 in 1995-96 to \$5,137 in 1998-99.

Using 1995-96 again as the base year which was the last full year that the former 27 school boards operated, school board expenditures declined by \$25.3 million, comprising \$17.8 million in instructional, \$5.3 million in administration, and \$2.2 million (net) in other expenditures. Expenditure on instruction per pupil increased 9% from \$3,841 in 1995-96 to \$4,173 in 1998-99. Figure 3 outlines the revenue and expenditures of the school boards for the year immediately before reorganization, the transition year and for the two years after reorganization.

### 3.17 Monitoring of School Boards

Figure 3

Department of Education  
School Boards  
Comparison of Financial Operations  
For the Years Ended 30 June  
(\$ 000's)

| Financial Item                                                   | Former<br>Boards | Transition | Current Boards |            |
|------------------------------------------------------------------|------------------|------------|----------------|------------|
|                                                                  | 1995-96          | 1996-97    | 1997-98        | 1998-99    |
| <b>Revenue</b>                                                   |                  |            |                |            |
| Provincial grants                                                |                  |            |                |            |
| Teachers                                                         | \$ 397,795       | \$ 376,178 | \$ 378,179     | \$ 379,304 |
| Regular operating                                                | 84,583           | 77,789     | 74,575         | 75,595     |
| Pupil transportation                                             | 30,264           | 29,345     | 27,666         | 26,846     |
| Other Provincial grants                                          | 4,073            | 4,590      | 4,691          | 7,921      |
| Total Provincial grants                                          | 516,715          | 487,902    | 485,111        | 489,666    |
| Federal grants                                                   | 4,649            | 4,826      | 5,090          | 4,158      |
| Ancillary services                                               | 1,811            | 1,330      | 985            | 1,032      |
| Miscellaneous revenue                                            | 6,536            | 5,441      | 5,608          | 5,509      |
| Total revenue                                                    | 529,711          | 499,499    | 496,794        | 500,365    |
| <b>Expenditure</b>                                               |                  |            |                |            |
| Administration                                                   | 18,730           | 15,792     | 14,573         | 13,441     |
| Instructional                                                    | 424,213          | 399,536    | 414,609        | 406,449    |
| Operations and maintenance                                       | 48,391           | 48,549     | 48,719         | 50,557     |
| Pupil transportation                                             | 29,270           | 30,060     | 28,331         | 28,001     |
| Ancillary services                                               | 490              | 579        | 490            | 692        |
| Miscellaneous                                                    | 615              | 299        | 167            | 182        |
| Debt repayment                                                   | 3,132            | 2,058      | 175            | 234        |
| Total expenditure                                                | 524,841          | 496,873    | 507,064        | 499,556    |
| Excess of revenue over expenditure<br>(expenditure over revenue) | 4,870            | 2,626      | (10,270)       | 809        |
| Transfer to capital                                              | (3,857)          | (4,991)    | (3,750)        | (3,330)    |
| Increase (decrease) in equity                                    | \$ 1,013         | \$ (2,365) | \$ (14,020)    | \$ (2,521) |

Source: School boards' audited financial statements, except unaudited 1998-99 figures for District 7.



### 3.17 Monitoring of School Boards

Figure 4

**Department of Education  
School Boards  
Summary of Financial Position  
30 June  
(\$ 000's)**

|                                     | Board         |               |               |               |               |               |               |               |               |                |            | Total          |                |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|----------------|------------|----------------|----------------|
|                                     | 1             | 2             | 3             | 4             | 5             | 6             | 7             | 8             | 9             | 10             | 11         | 1999           | 1998           |
| <b>Current Assets</b>               |               |               |               |               |               |               |               |               |               |                |            |                |                |
| Cash and investments                | -             | -             | -             | -             | 1,316         | -             | -             | -             | 970           | 3,280          | 90         | 5,616          | 6,054          |
| Accounts receivable                 | 4,212         | 675           | 1,150         | 546           | 537           | 1,250         | 1,110         | 378           | 627           | 1,826          | 185        | 12,505         | 9,304          |
| Other assets                        | 36            | 21            | 2             | 48            | 87            | 145           | 179           | 89            | 94            | 248            | 7          | 958            | 989            |
| <b>Total current assets</b>         | <b>4,250</b>  | <b>696</b>    | <b>1,152</b>  | <b>594</b>    | <b>1,940</b>  | <b>1,404</b>  | <b>1,289</b>  | <b>467</b>    | <b>1,691</b>  | <b>5,354</b>   | <b>242</b> | <b>19,079</b>  | <b>16,347</b>  |
| <b>Capital assets</b>               | <b>41,430</b> | <b>37,585</b> | <b>55,167</b> | <b>73,178</b> | <b>71,394</b> | <b>73,775</b> | <b>43,559</b> | <b>36,258</b> | <b>34,966</b> | <b>105,876</b> | <b>225</b> | <b>613,413</b> | <b>622,027</b> |
| <b>Total assets</b>                 | <b>45,680</b> | <b>38,281</b> | <b>56,319</b> | <b>73,772</b> | <b>73,334</b> | <b>75,179</b> | <b>44,848</b> | <b>36,725</b> | <b>36,657</b> | <b>111,230</b> | <b>467</b> | <b>632,492</b> | <b>638,374</b> |
| <b>Current Liabilities</b>          |               |               |               |               |               |               |               |               |               |                |            |                |                |
| Bank indebtedness                   | 127           | 518           | 1,114         | 3             | -             | 60            | 1,971         | 548           | -             | -              | -          | 4,341          | 2,828          |
| Accounts payable                    | 4,166         | 210           | 344           | 555           | 1,316         | 1,226         | 1,024         | 90            | 1,208         | 2,111          | 157        | 12,495         | 10,209         |
| Current maturities                  | 75            | 6             | 86            | -             | 693           | 326           | 6             | 18            | -             | -              | -          | 1,210          | 1,015          |
| <b>Total current liabilities</b>    | <b>4,368</b>  | <b>742</b>    | <b>1,544</b>  | <b>558</b>    | <b>2,009</b>  | <b>1,612</b>  | <b>3,001</b>  | <b>656</b>    | <b>1,298</b>  | <b>2,111</b>   | <b>157</b> | <b>18,046</b>  | <b>14,052</b>  |
| <b>Long-term debt</b>               | <b>504</b>    | <b>68</b>     | <b>553</b>    | <b>-</b>      | <b>193</b>    | <b>674</b>    | <b>75</b>     | <b>655</b>    | <b>-</b>      | <b>-</b>       | <b>-</b>   | <b>2,722</b>   | <b>1,411</b>   |
| <b>Severance pay</b>                | <b>4,671</b>  | <b>4,024</b>  | <b>9,028</b>  | <b>7,191</b>  | <b>10,798</b> | <b>9,813</b>  | <b>5,232</b>  | <b>4,695</b>  | <b>10,591</b> | <b>26,700</b>  | <b>167</b> | <b>92,903</b>  | <b>90,646</b>  |
| <b>Total liabilities</b>            | <b>9,543</b>  | <b>4,834</b>  | <b>11,125</b> | <b>7,749</b>  | <b>13,000</b> | <b>12,099</b> | <b>8,308</b>  | <b>5,999</b>  | <b>11,879</b> | <b>28,811</b>  | <b>324</b> | <b>113,671</b> | <b>106,109</b> |
| <b>Equity</b>                       |               |               |               |               |               |               |               |               |               |                |            |                |                |
| Investment                          | 41,107        | 37,510        | 54,526        | 73,179        | 70,487        | 73,345        | 43,280        | 35,578        | 34,966        | 105,227        | 225        | 609,432        | 620,346        |
| Deficit                             | (4,970)       | (4,063)       | (9,334)       | (7,156)       | (10,153)      | (10,265)      | (6,740)       | (4,852)       | (10,188)      | (22,808)       | (82)       | (90,611)       | (88,081)       |
| <b>Total equity</b>                 | <b>36,137</b> | <b>33,447</b> | <b>45,194</b> | <b>66,023</b> | <b>60,334</b> | <b>63,080</b> | <b>36,540</b> | <b>30,726</b> | <b>24,778</b> | <b>82,419</b>  | <b>143</b> | <b>518,821</b> | <b>532,265</b> |
| <b>Total liabilities and equity</b> | <b>45,680</b> | <b>38,281</b> | <b>56,319</b> | <b>73,772</b> | <b>73,334</b> | <b>75,179</b> | <b>44,848</b> | <b>36,725</b> | <b>36,657</b> | <b>111,230</b> | <b>467</b> | <b>632,492</b> | <b>638,374</b> |

Source: 31 March 1999 Audited Financial Statements, except for District 7, which were based on unaudited financial statements.

### 3.17 Monitoring of School Boards

Figure 4

**Department of Education  
School Boards  
Summary of Financial Position  
30 June  
(\$ 000's)**

|                                     | Board         |               |               |               |               |               |               |               |               |                |            | Total          |                |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|----------------|------------|----------------|----------------|
|                                     | 1             | 2             | 3             | 4             | 5             | 6             | 7             | 8             | 9             | 10             | 11         | 1999           | 1998           |
| <b>Current Assets</b>               |               |               |               |               |               |               |               |               |               |                |            |                |                |
| Cash and investments                | -             | -             | -             | -             | 1,316         | -             | -             | -             | 970           | 3,280          | 50         | 5,616          | 6,064          |
| Accounts receivable                 | 4,212         | 675           | 1,150         | 546           | 537           | 1,259         | 1,110         | 378           | 627           | 1,826          | 185        | 12,505         | 9,304          |
| Other assets                        | 38            | 21            | 2             | 48            | 87            | 145           | 179           | 89            | 94            | 248            | 7          | 958            | 989            |
| <b>Total current assets</b>         | <b>4,250</b>  | <b>696</b>    | <b>1,152</b>  | <b>594</b>    | <b>1,940</b>  | <b>1,404</b>  | <b>1,289</b>  | <b>467</b>    | <b>1,691</b>  | <b>5,354</b>   | <b>242</b> | <b>19,079</b>  | <b>16,347</b>  |
| <b>Capital assets</b>               | <b>41,430</b> | <b>37,585</b> | <b>55,167</b> | <b>73,178</b> | <b>71,394</b> | <b>73,775</b> | <b>43,559</b> | <b>36,258</b> | <b>74,966</b> | <b>105,876</b> | <b>225</b> | <b>613,413</b> | <b>622,027</b> |
| <b>Total assets</b>                 | <b>45,680</b> | <b>38,281</b> | <b>56,319</b> | <b>73,772</b> | <b>73,334</b> | <b>75,179</b> | <b>44,848</b> | <b>36,725</b> | <b>76,657</b> | <b>111,230</b> | <b>467</b> | <b>632,492</b> | <b>638,374</b> |
| <b>Current Liabilities</b>          |               |               |               |               |               |               |               |               |               |                |            |                |                |
| Bank indebtedness                   | 127           | 518           | 1,114         | 3             | -             | 60            | 1,971         | 548           | -             | -              | -          | 4,341          | 2,828          |
| Accounts payable                    | 4,166         | 218           | 344           | 555           | 1,316         | 1,226         | 1,024         | 90            | 1,288         | 2,111          | 157        | 12,495         | 10,209         |
| Current maturities                  | 75            | 6             | 86            | -             | 693           | 326           | 6             | 18            | -             | -              | -          | 1,210          | 1,015          |
| <b>Total current liabilities</b>    | <b>4,368</b>  | <b>742</b>    | <b>1,544</b>  | <b>558</b>    | <b>2,009</b>  | <b>1,612</b>  | <b>3,001</b>  | <b>656</b>    | <b>1,288</b>  | <b>2,111</b>   | <b>157</b> | <b>18,046</b>  | <b>14,052</b>  |
| <b>Long-term debt</b>               | <b>504</b>    | <b>68</b>     | <b>553</b>    | <b>-</b>      | <b>193</b>    | <b>674</b>    | <b>75</b>     | <b>655</b>    | <b>-</b>      | <b>-</b>       | <b>-</b>   | <b>2,722</b>   | <b>1,411</b>   |
| <b>Severance pay</b>                | <b>4,671</b>  | <b>4,024</b>  | <b>9,028</b>  | <b>7,191</b>  | <b>10,798</b> | <b>9,813</b>  | <b>5,232</b>  | <b>4,688</b>  | <b>10,591</b> | <b>26,700</b>  | <b>167</b> | <b>92,903</b>  | <b>90,646</b>  |
| <b>Total liabilities</b>            | <b>9,543</b>  | <b>4,834</b>  | <b>11,125</b> | <b>7,749</b>  | <b>13,000</b> | <b>12,099</b> | <b>8,308</b>  | <b>5,999</b>  | <b>11,879</b> | <b>28,811</b>  | <b>324</b> | <b>113,671</b> | <b>106,109</b> |
| <b>Equity</b>                       |               |               |               |               |               |               |               |               |               |                |            |                |                |
| Investment                          | 41,107        | 37,510        | 54,528        | 73,179        | 70,487        | 73,345        | 43,280        | 35,578        | 74,966        | 105,227        | 225        | 609,432        | 620,346        |
| Deficit                             | (4,970)       | (4,063)       | (9,334)       | (7,156)       | (10,153)      | (10,265)      | (6,740)       | (4,852)       | (10,188)      | (22,808)       | (82)       | (90,611)       | (88,081)       |
| <b>Total equity</b>                 | <b>36,137</b> | <b>33,447</b> | <b>45,194</b> | <b>66,023</b> | <b>60,334</b> | <b>63,080</b> | <b>36,540</b> | <b>30,726</b> | <b>64,778</b> | <b>82,419</b>  | <b>143</b> | <b>518,821</b> | <b>532,265</b> |
| <b>Total liabilities and equity</b> | <b>45,680</b> | <b>38,281</b> | <b>56,319</b> | <b>73,772</b> | <b>73,334</b> | <b>75,179</b> | <b>44,848</b> | <b>36,725</b> | <b>76,657</b> | <b>111,230</b> | <b>467</b> | <b>632,492</b> | <b>638,374</b> |

Source: 31 March 1999 Audited Financial Statements, except for District 7, which were based on unaudited financial statements.



### **3.17 Monitoring of School Boards**

#### **Department's Response**

##### ***Financial Position***

*The Department has been closely monitoring the financial performance of school boards to ensure that any operating deficits are addressed by the boards in a timely manner, with a view to eliminating any accumulated deficit as soon as possible.*

*The Department notes that of the six boards which had accumulated deficits at June 30, 1999, three had made progress to reduce the total amount from the June, 1998 level. In the case of those three boards with growing deficits as of June 30, 1999, the Department has initiated discussions with each to ensure that appropriate measures are taken to reduce these deficits. In the case of District 7, the board with by far the most serious deficit situation, the Department is maintaining an ongoing dialogue on the matter, resulting in significant progress.*

##### ***Compliance with Legislation***

*The Department is committed to ensuring that boards comply with all relevant legislation. For 1999/2000, follow up is being undertaken for those boards which have been late in submitting budgets. The Department will be advising boards that any projected deficits must be identified as quickly as possible, with a plan for corrective action to ensure that a deficit is not incurred at year end.*

##### ***Operating Results***

*The principal cause of the decline in revenues and expenditures over the 1995-96 to 1998-99 period relates to reductions in the number of teachers in the system. The Department notes that while the number of teachers (FTE) has declined from 7,259 to 6,453 (11%) over the period, the decline in student enrolment over the same period was from 110,456 to 97,401 (12%).*

*The other major reasons for the decline in expenditures relate to administrative efficiencies achieved in the reduction from 27 to 11 school boards; efficiencies in pupil transportation related to school closures; and, reductions in debt repayment due to retirement of accrued deficits of the old boards at the time of reorganization.*

*Funding for operations and maintenance, and for instruction exclusive of teacher payroll, has been increased over the period.*

### 3.18 A Review of the Multi-Materials Stewardship Board

#### Introduction

On 15 January 1997, Government implemented a Beverage Container Control Program in the Province. Under this program, the consumer pays a deposit of 6 cents on the price of a ready-to-serve non-alcohol beverage container and 20 cents on an alcohol beverage container. Upon returning a beverage container to one of the 37 established depots in the Province, consumers receive a refund of 3 cents on a non-alcohol beverage container and 10 cents on an alcohol beverage container. These containers are then transported from the depots to centres for processing. Figure 1 provides information on the locations of the depots throughout the Province.

**Figure 1**

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#### Depot locations



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Source: Multi-Materials Stewardship Board

### 3.18 A Review of the Multi-Materials Stewardship Board

In addition to paying refunds to consumers, deposits, along with proceeds from the sale of collected containers, are used to support the operating costs of the Beverage Container Control Program. All excess monies are to be paid into the Newfoundland and Labrador Waste Management Trust Fund as directed by Government. This trust fund was established pursuant to the *Packaging Materials Act* for the purpose of providing funds for Government-approved waste management initiatives.

To manage the Beverage Container Control Program and the Waste Management Trust Fund, Government established the Multi-Materials Stewardship Board on 18 June 1996 pursuant to the *Packaging Materials Act*. The Board's mandate is to support and promote the protection, enhancement and wise use of the environment through waste management programs. On an annual basis, the Board is required to submit to the Minister of Environment and Labour both an operating budget for approval and a report on Board activities and results of financial operations for the previous year. The Board consists of 10 voting members appointed by the Minister of Environment and Labour as follows:

- one consumer representative;
- one representative from distributors of beverage containers;
- one representative from the Department of Environment and Labour;
- one representative from the Department of Industry, Trade and Technology;
- one representative from the Department of Municipal and Provincial Affairs; and
- five representatives at large chosen by the Minister of Environment and Labour.

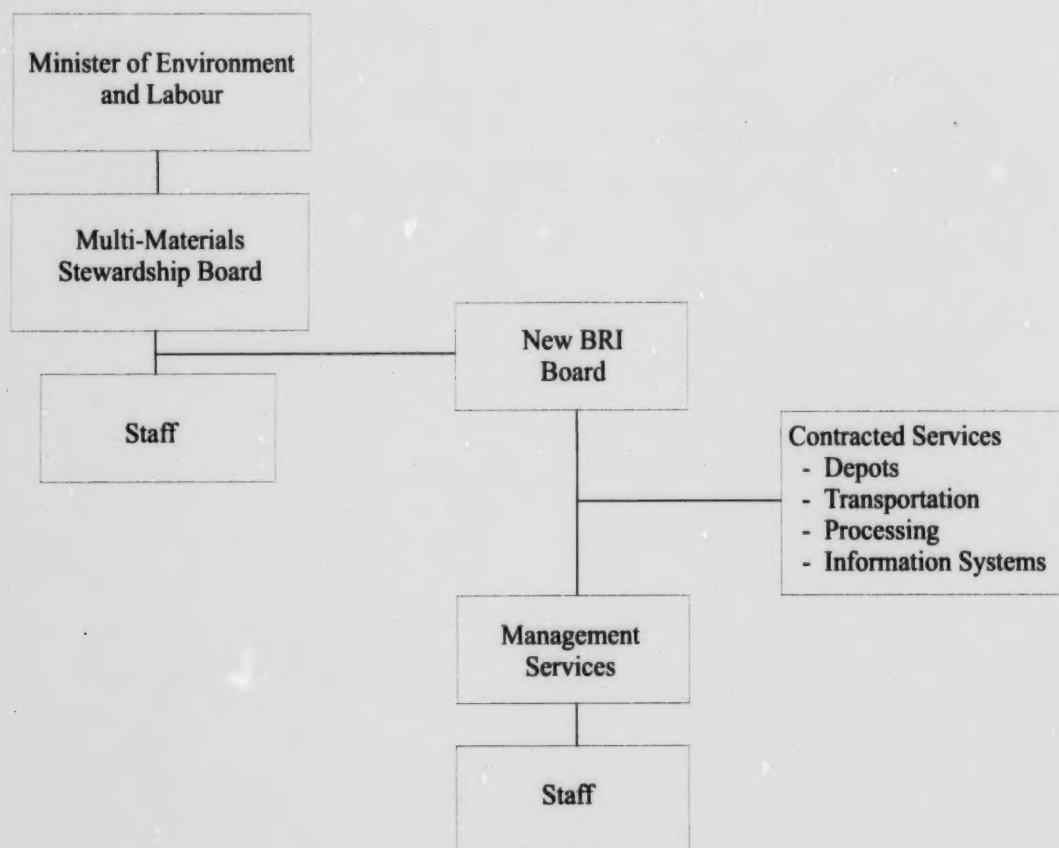
On 8 September 1997, under the provisions of the *Beverage Container Control Regulations*, the Multi-Materials Stewardship Board entered into an agreement with Newfoundland Beverage Recovery Inc. (NewBRI) to operate, maintain and manage the Beverage Container Control Program on behalf of the Multi-Materials Stewardship Board. The Agreement covers the period from 8 November 1996, the date NewBRI had effectively been operating the Program, until 15 January 2002.

### 3.18 A Review of the Multi-Materials Stewardship Board

NewBRI is a not-for-profit corporation established by the beverage industry for the purpose of carrying out the responsibilities of this Agreement. The Multi-Materials Stewardship Board, however, retains legislative responsibility for the Program and as a result, the Agreement contains provision for the Board to monitor NewBRI's management of the Program. During the initial implementation of this Program in January of 1997 until the Multi-Materials Stewardship Board assumed control in April 1997, the Department of Environment and Labour managed the Program. The structure for the management of the Program is outlined in Figure 2.

**Figure 2**

#### **Management Structure Beverage Container Control Program**



### 3.18 A Review of the Multi-Materials Stewardship Board

Under this structure, distributors of beverage containers remit the deposits to NewBRI. These deposits are used for program operations, including the operation of the Multi-Materials Stewardship Board. NewBRI holds all excess monies until directed by Government to pay the funds into the Newfoundland and Labrador Waste Management Trust Fund. In July 1999, Cabinet directed that funding of \$3 million of the approximately \$7 million at NewBRI be transferred to the Trust Fund.

Information on the Multi-Materials Stewardship Board's revenue and expenditure for the years ended 31 March 1998 and 31 March 1999 is presented in Figure 3.

Figure 3

#### Multi-Materials Stewardship Board Revenue and Expenditure 31 March

|                                           | 1998            | 1999            | Total           |
|-------------------------------------------|-----------------|-----------------|-----------------|
| <b>Revenue</b>                            |                 |                 |                 |
| From NewBRI for operations                | \$300,000       | \$325,000       | \$625,000       |
| From NewBRI for marketing                 | -               | 217,000         | 217,000         |
| Interest                                  | 325             | 11,415          | 11,740          |
|                                           | 300,325         | 553,415         | 853,740         |
| <b>Expenditures</b>                       |                 |                 |                 |
| Marketing & Communications                | 53,946          | 243,805         | 297,751         |
| Salaries & Benefits                       | 90,272          | 157,136         | 247,408         |
| Rent                                      | 8,000           | 32,640          | 40,640          |
| Travel                                    | 35,884          | 19,295          | 55,179          |
| Office & Telecommunications               | 14,803          | 14,961          | 29,764          |
| Directors Remuneration                    | 12,143          | 11,494          | 23,637          |
| Consulting & Professional Fees            | 58,048          | 8,748           | 66,796          |
| Meetings & Entertainment                  | 2,393           | 4,405           | 6,798           |
| Other                                     | 7,807           | 21,181          | 28,988          |
|                                           | 283,296         | 513,665         | 796,961         |
| <b>Excess of revenue over expenditure</b> | <b>\$17,029</b> | <b>\$39,750</b> | <b>\$56,779</b> |

Source: Audited Financial Statements

### 3.18 A Review of the Multi-Materials Stewardship Board

Summary financial information on NewBRI's operations for the years ended 31 March 1998 and 31 March 1999 is presented in Figure 4.

#### Scope and Objectives

We commenced our review of the Beverage Container Control Program in October of 1999. The objectives of our review were to:

- determine whether the Board has adequate policies and procedures for managing the Beverage Container Control Program, including procedures to monitor the operations of Newfoundland Beverage Recovery Inc;
- review the investment policy for the Waste Management Trust Fund and determine if monies disbursed from the Fund are in accordance with established program guidelines; and
- review Board expenditures and practices to assess compliance with Government legislation and policies.

Figure 4

#### Newfoundland Beverage Recovery Inc. Summary Financial Information (\$ Millions)

|                                                   | 1998   | 1999   | Total  |
|---------------------------------------------------|--------|--------|--------|
| Results of Operation                              |        |        |        |
| Total Revenues                                    | \$11.4 | \$11.8 | \$23.2 |
| Total Expenditures                                | 8.1    | 7.9    | 16.0   |
| Net Earnings, 31 March                            | \$3.3  | \$3.9  | \$7.2  |
| Financial Position                                |        |        |        |
| Total Assets                                      | \$4.4  | \$7.8  |        |
| Total Liabilities                                 | 1.0    | .8     |        |
| Total Net Assets, 31 March                        | \$3.4  | \$7.0  |        |
| Transfer to Government's Trust Fund, October 1999 |        | (3.0)  |        |
| Balance                                           |        | \$4.0  |        |

Source: Audited Financial Statements and Multi-Materials Stewardship Board records



### 3.18 A Review of the Multi-Materials Stewardship Board

#### Conclusions

In June 1996, Government established the Multi-Materials Stewardship Board to manage the Beverage Container Control Program and a Waste Management Trust Fund.

On 15 January 1997 Government implemented a Beverage Container Control Program in which consumers pay a deposit on beverage containers and receive a refund upon returning the containers. In addition to paying refunds, deposits, along with proceeds from the sale of collected containers are used to support the operating costs of the Beverage Container Control Program. All excess monies are to be paid into the Waste Management Trust Fund to be used to provide funds for Government-approved waste management initiatives.

As of 31 March 1999, net assets of Newfoundland Beverage Recovery Inc. totalled approximately \$7.0 million. In July 1999, Cabinet directed that \$3.0 million of the \$7.0 million at Newfoundland Beverage Recovery Inc. be transferred to the Waste Management Trust Fund to be used for the purpose of supporting community-based environmental initiatives, such as community clean-ups, recycling and environmental education programs.

Our review indicated that the Multi-Materials Stewardship Board is adequately monitoring the management of the Beverage Container Control Program. However, several significant issues were identified during our review:

- In 1996, Government established target recovery rates for beverage containers sold at 50% for 1997, 60% for 1998, 70% for 1999, and 80% for 2000. Our review in November 1999 found that the target recovery rate has stagnated at approximately 50%. A consultant has recently been contracted to review the effectiveness of the Beverage Container Control Program.
- In September 1997, the Multi-Materials Stewardship Board entered into an agreement with Newfoundland Beverage Recovery Inc. to operate, maintain and manage the Beverage Container Control Program on behalf of the Board. Under the Agreement, the Board has the right to inspect and audit all the records of the Newfoundland Beverage Recovery Inc. The Board has not exercised its right to inspect and audit those records as they relate to expenditures. This is significant since annual expenditures are approximately \$8.0 million.
- The Newfoundland Beverage Recovery Inc. is not submitting an annual budget and work plan for Program activities for approval of the Board as required under the Agreement between the Newfoundland Beverage Recovery Inc. and the Board.

### 3.18 A Review of the Multi-Materials Stewardship Board

Our review of the Waste Management Trust Fund indicated the following;

- The Multi-Materials Stewardship Board has not established an investment policy for the funds on deposit at the Newfoundland Beverage Recovery Inc. or for the funds maintained in the Waste Management Trust Fund.
- The Waste Management Trust Fund is to be used for the purpose of supporting community-based environmental initiatives, such as community clean-ups, recycling and environmental education programs. Funding is available for several categories of projects and a Committee established by Cabinet, comprised of the Minister of Environment and Labour, the Minister of Municipal and Provincial Affairs, the Minister of Development and Rural Renewal, and the Minister of Tourism, Culture and Recreation, in conjunction with the Board determines the total funding allocated to each category. The Board recommends to the Minister of Environment and Labour the individual projects to be funded. The Board has recently expressed its concern to the Minister regarding the significant re-allocation of project funding among the various categories.
- At the end of our review in November 1999, 45 projects totalling \$873,700 had been recommended for funding by the Board and approved by the Minister of Environment and Labour. Our review of a sample of these applications determined that they met established program criteria, and approved funding was determined in accordance with Program guidelines. We also determined that reasons for approving or rejecting applications were adequately documented by the Board.
- Two instances were identified where the Board, based on the application of the program guidelines and eligibility criteria, made recommendations on a course of action regarding project funding requests which were not accepted by the Minister of Environment and Labour. Although the Minister, under the *Waste Management Regulations*, can accept or reject the Board's funding recommendations, there was no documentation provided to the Board to support the rationale for the final decision. Such information would be of assistance to the Board in ensuring consistent application of Program guidelines and establishing future funding levels.
- Prior to advancing approved funding to project sponsors, sponsors are required to provide documentation to confirm their required percentage share of the project costs. For two of the six files examined where funds have been advanced, we determined that

### 3.18 A Review of the Multi-Materials Stewardship Board

the share confirmed as being contributed by the project sponsor was less than the amount required under Program guidelines. For one of these same two projects, the funding approved was substantially less than the funding requested in the original application but there was no documentation provided to indicate how the remaining required project funding would be funded.

In reviewing Board operations, it was determined that the Board has not submitted an annual report on operations for 1998-99 to the Minister of Environment and Labour as required by the *Beverage Container Control Regulations* (repealed and replaced by the *Waste Management Regulations* in October of 1999).

#### Findings and Recommendation

#### Management of the Beverage Container Control Program

Although NewBRI operates the Beverage Container Control Program, the Multi-Materials Stewardship Board retains legislative responsibility for the Program and therefore, it is essential that the Board is adequately monitoring NewBRI's management of the Program. Our review of this area indicated the following:

##### 1. Monitoring of NewBRI operations

The Agreement between the Board and NewBRI contains the following provisions to enable the Board to monitor NewBRI's management of the Beverage Container Control Program:

- On a monthly basis, NewBRI is required to submit financial statements and production statistics on the collection of beverage containers to the Board. Our review indicated that NewBRI is submitting monthly financial statements and production statistics to the Board as required under the Agreement.
- On an annual basis, NewBRI is required to submit its budget and workplan for approval by the Board. As the Board retains legislative responsibility for the Beverage Container Control Program, it is essential that the Board be aware of NewBRI's planned Program activities and its anticipated revenues and expenditures. Our review indicated that NewBRI has not submitted an annual budget or work plan of Program activities to the Board for approval as required under the Agreement.

### **3.18 A Review of the Multi-Materials Stewardship Board**

- The Chairperson of the Multi-Materials Stewardship Board is to be appointed to the NewBRI board. Our review indicated that the Chairperson of the Multi Materials Stewardship Board was appointed to the NewBRI Board in September of 1997.
- The Board has the right to inspect and audit all of NewBRI records. Our review indicated that the Board has on staff a compliance officer whose responsibilities include ensuring that all beverage container distributors have been identified, that these distributors have registered all types of eligible beverage containers that they sell and that these distributors are remitting the correct amount of deposits to NewBRI on a timely basis. This work conducted by the Board helps ensure that the appropriate revenue is being received and reported by NewBRI. Although the revenues of NewBRI are being audited, the Board has not exercised its right to inspect and audit records of NewBRI as they relate to expenditures. The Board receives NewBRI's annual audited financial statements.

#### **2. Target Recovery Rates**

In implementing the Beverage Container Control Program, Government established target recovery rates for beverage containers sold at 50% for 1997, 60% for 1998, 70% for 1999 and 80% for 2000. Included in the Agreement between the Multi-Materials Stewardship Board and NewBRI is a provision by NewBRI to take reasonable steps to achieve the recovery rates outlined above. Our review in November 1999, however, found that the actual recovery rates have stagnated at approximately 50%.

A survey of the general public conducted by the Multi-Materials Stewardship Board in 1998 indicated that some of the reasons for this lower than expected recovery rate included a lack of interest in recycling by the public, a low refund rate on beverage containers and a lack of accessibility to depots. In an attempt to improve these rates, NewBRI provided \$217,000 to the Board in 1998/99 for marketing initiatives for the Program.

In September 1999, the Multi-Materials Stewardship Board requested the Minister of Environment and Labour to make regulatory amendments that would result in an increase in the consumer refund from 3 cents to 4 cents for non-alcohol containers and from 10 cents to 12 cents for alcohol beverage containers. The Minister indicated that he could not recommend this refund increase to Cabinet until he received clearer information that such an increase in the consumer refund rate would result in increased return rates over other options that may be available.

### **3.18 A Review of the Multi-Materials Stewardship Board**

NewBRI and the Board recently developed terms of reference for an evaluation of the effectiveness of the Program and selected a consultant to conduct this review based on proposals received as a result of a public call for proposals. This contract is estimated to cost approximately \$50,000.

#### **Waste Management Trust Fund**

As shown in Figure 4, net assets of NewBRI at 31 March 1999 are approximately \$7 million. In July 1999, Cabinet directed that funding of \$3 million be transferred from NewBRI operations to the Waste Management Trust Fund. These funds are to be used for the purpose of supporting community-based environmental initiatives such as community clean-ups, recycling programs and environmental education programs. At this time, Cabinet also established a Committee comprised of the Minister of Environment and Labour, the Minister of Municipal and Provincial Affairs, the Minister of Development and Rural Renewal, and the Minister of Tourism, Culture and Recreation to develop a process and criteria for approving projects to be funded from the Trust Fund.

We reviewed the Board's investment policies with respect to the Trust Fund and also reviewed the procedures used by the Board to ensure that excess funds still held by NewBRI are being invested properly. We also examined a selection of approved applications that received funding from the Trust Fund to ensure that applications met established program guidelines. Our review of these areas indicated the following:

##### **1. Investment Policy**

Monies held in the Waste Management Trust Fund bank account are earning a rate of prime less 1.95%. We were advised by Board staff that excess funds at NewBRI are on deposit with their banker under the same arrangement. Board staff have also informed us that they have been in communication with Government officials who offered to manage the trust monies on behalf of the Board; however, no decision has been made with respect to an investment advisor. As the Board has not yet developed an investment policy, it may not be maximizing the return on the Trust Fund.

##### **2. Disbursements from the Trust Fund**

In September 1999, Government announced that in reference to the \$3 million allocated to the Trust Fund in July 1999 for community-based environmental initiatives, applications would be received and evaluated by the Board and that the Board would accept applications up to 29 October 1999. The announcement also indicated that applications would be approved on an on-going basis even before the 29 October deadline.



### 3.18 A Review of the Multi-Materials Stewardship Board

Under program guidelines, applications can be approved in one of seven areas as indicated in Figure 5.

Figure 5

#### Waste Management Trust Fund Funding Categories and Funding Levels

| Funding Category                                                                                                                   | Funding Levels                                                                                                                                                                                                  |
|------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Development of a municipal, institutional or regional recycling program which supports existing programs approved by the Minister. | Not exceeding 75% of total project cost to a maximum contribution of \$50,000.                                                                                                                                  |
| Planning, development and upgrading of a regional or municipal waste management system.                                            | Planning for individual and regional waste management systems will be funded up to 50% and 100% of total cost respectively. Development costs for all waste management systems will be funded on a 50/50 basis. |
| Workshops, seminars or educational or promotional programs or activities which would enhance waste management.                     | Not exceeding 75% of total project cost to a maximum of \$50,000.                                                                                                                                               |
| Community Service groups, municipalities, schools and others for waste material cleanup activities.                                | Not exceeding 75% of total project cost to a maximum of \$25,000.                                                                                                                                               |
| Government or Multi-Materials Stewardship Board initiatives for waste management.                                                  | Government - Not exceeding 75% of total project cost to a maximum of \$100,000.<br><br>Board - Up to 100% of total project cost to a maximum of \$100,000.                                                      |
| Investigation and demonstration of new technologies that would enhance waste management.                                           | Not exceeding 50% of total project cost to a maximum of \$50,000.                                                                                                                                               |
| Market analysis and feasibility studies related to business development opportunities resulting from a waste management activity.  | Not exceeding 50% of total project cost to a maximum of \$50,000.                                                                                                                                               |

Source: Program Guidelines



### 3.18 A Review of the Multi-Materials Stewardship Board

Adequate policies and procedures are necessary to ensure that approved applications are those most likely to achieve program objectives. This would include reviewing the applications to ensure established eligibility and selection criteria are met and adequately documenting the reasons why applications are approved or rejected.

We were informed that the Committee established by Cabinet which was comprised of the Minister of Environment and Labour, the Minister of Municipal and Provincial Affairs, the Minister of Development and Rural Renewal, and the Minister of Tourism, Culture and Recreation, in conjunction with staff of the Board, developed the process and criteria for approving projects to be funded from the Trust Fund.

The Board has a Trust Fund Administrator who reviews applications received to ensure that they qualify for funding under the Program guidelines. These applications are then forwarded to the Board for their assessment. Once applications are reviewed by the Board, a listing of applicants with summary information on the project, along with the Board's recommendation on the various project applications, is forwarded to the Minister of Environment and Labour for final assessment and approval.

At the end of our review in November 1999, 45 projects totalling \$873,700 had been recommended for funding by the Board and approved by the Minister of Environment and Labour. We also noted that there were 10 applications that had been rejected for funding by the Board and the Minister and there are 146 applications requesting funds totalling \$4,818,528 not yet processed. Our review of 12 approved applications and the 10 rejected applications indicated the following:

- Applications recommended for approval by the Board met established program criteria and approved funding was determined in accordance with Program guidelines. We also determined that reasons for approving or rejecting applications were adequately documented by the Board.
- A review of rejected applications indicated that they did not meet eligibility criteria for the Program (i.e. constructing ATV trails, etc.). We did note, however, that one of the applications in the amount of \$25,108 which was recommended for rejection by the Board was subsequently approved by the Minister of Environment and Labour as allowed under the *Waste Management Regulations*. The Board staff indicated that no documentation was provided to the Board as to why this project was approved by the Minister. Such information provided to the Board would help ensure consistent application of Program guidelines.

### **3.18 A Review of the Multi-Materials Stewardship Board**

- One of the projects recommended for funding by the Board had projected costs of \$24,702 of which the Board recommended funding of \$18,527 or 75% of total costs as outlined in the Program guidelines. The Minister of Environment and Labour, however, subsequently increased the approved funding to 100% of project costs or \$24,702. Staff of the Board indicate that no documentation was provided to the Board to support the increase in approved funding. Again, such information would be of assistance to the Board when it is establishing future funding levels.

We also reviewed a copy of the standard Contribution Agreement and any additional documentation that had been returned to the Board by the approved project sponsors. This Agreement outlines the terms and conditions of the approved funding including payment conditions and audit and evaluation requirements for the project. At the time of completion of our review in November there were six signed Contribution Agreements returned from approved applicants for which the Board had advanced funding.

A review of these six Contribution Agreements and advances indicated that, under the Contribution Agreement, sponsors are required to provide documentation to confirm their required percentage share of the project costs. For two of the six files examined where funds have been advanced, we determined that the share confirmed as being contributed by the project sponsor was less than the amount required under Program guidelines. For one of these same two projects, the funding approved was substantially less than the funding requested in the original application but there was no documentation provided to indicate how the remaining required project funding would be funded.

#### **3. Trust Fund Allocation**

The Multi-Materials Stewardship Board has expressed concern to the Minister regarding the significant re-allocation of project funding. For example, funding for clean-up projects has been increased significantly from \$780,000 to \$1.6 million by reducing funding for other purposes. The \$1.6 million for clean-up projects was to be paid from the \$3 million available in the Trust Fund for all categories of projects. The Board was of the opinion that it was unfair to allocate such a high level of funding for clean-up before assessing proposals in the other categories such as developing various recycling programs, waste management systems, and seminars and promotional programs. The Board also felt that there were good environmental projects in these other categories that could potentially result in sustainable employment opportunities, and that the re-allocation would impede the Board's ability to pursue its legislative

### 3.18 A Review of the Multi-Materials Stewardship Board

mandate. Our discussions with Departmental officials indicate that such funding re-allocations reflect Government priorities.

#### Board Operations

During our review we determined that the Board has not submitted an annual report on operations for 1998-99 to the Minister of Environment and Labour as required by the *Beverage Container Control Regulations* (repealed and replaced by the *Waste Management Regulations* in October of 1999).

We also reviewed the expenditures of the Board for the years ended 31 March 1998 and 31 March 1999 to determine whether the Board was complying with Government legislation and policies. Our review of this area indicated the following:

- Board members were appointed early in 1997 and the Chair in September of 1997. The Minister of Environment and Labour directed that the Board follow Government's policy with respect to Board member remuneration. Board remuneration for the years ended 31 March 1998 and 31 March 1999 was \$12,143 and \$11,494 respectively. A review of these expenditures indicated that one of the Board members received \$9,995 of the \$12,143 and \$7,885 of the \$11,494.

Government's Board Remuneration Policy provides remuneration for preparation for and attendance at Board meetings. A review of the payments of \$9,995 and \$7,885 paid to one Board member indicated that there was insufficient information to determine what type of work the payment was for and thus, whether this Board member should have been remunerated for this work.

- Although the Board indicated that they determined a reasonable and fair price for the acquisition of goods and services under \$7,500 (\$10,000 after June 1998), documentation of this process was not maintained on file. As a result, we could not determine whether or not the Board adhered to the *Public Tender Act*. After February 1999, the Board has complied with the *Public Tender Act* with respect to obtaining quotes for goods and services under \$10,000.

### **3.18 A Review of the Multi-Materials Stewardship Board**

- The Board has adopted Treasury Board Guidelines as policy for Board member and staff travel. A sample of 9 travel claims were examined to determine compliance with Board travel guidelines and we found that in 3 instances, although the amounts claimed were in accordance with Government's travel rules, the claim was not approved. In another instance the entertainment expense exceeded Board policy and was not approved by the Board Chair.

#### **Conflict of Interest**

Our review identified two possible conflict of interest situations. We recommended that the Board refer these matters to the Conflict of Interest Tribunal.

#### **Recommendation**

*The Board should consider the issues raised in this report and take appropriate action.*

#### **Board's Response**

#### **Management of the Beverage Recovery Program**

##### **Monitoring of NewBRI Operations**

*With respect to monitoring the expenditures of NewBRI, there are a number of controls in place. In addition to the monthly financial reports, the MMSB Chairman is a voting member of NewBRI's Board. As well, an excellent working relationship exists between the offices of MMSB and NewBRI. Consequently, the MMSB office is kept abreast of NewBRI's operations on an ongoing basis.*

*Aside from any extraordinary expenses, for which NewBRI would seek approval from MMSB, other expenditures would be only for routine operational aspects of the beverage recovery system. Thus, annual budget categories and program activities remain somewhat constant from year to year. Financial projections that have been prepared in the past have detailed costs associated with various recovery rates. Such projections have been reviewed by the Board. The MMSB will in the future, however, require that NewBRI supply the information as outlined in the Agreement.*

### **3.18 A Review of the Multi-Materials Stewardship Board**

#### ***Waste Management Trust Fund***

##### ***Investment Policy***

*While no formal policy dealing with risk levels and return rates was adopted, it was accepted that any investing from the Trust Fund would be in accordance with the Financial Administration Act. The present rate of prime less 1.95% on the Fund earns interest at a rate of approximately 4-5 percent. This rate is comparable to present rates on Guaranteed Income Certificates which would be the type of low risk investment made in accordance with the Financial Administration Act. It was expected that money from the Fund would be disbursed to applicants over a relatively short period; consequently, accessibility was an issue. At present, approximately one-half of the total funding has been committed to projects. Of this money, some 66 percent will be expended by March 31, 2000.*

*The same rate of prime less 1.95 percent is earned on the beverage recovery operating funds. For both accounts the MMSB will attempt to determine whether or not a better interest rate can be obtained for both these accounts.*

##### ***Disbursements***

*Adjustments to the funding contribution for any application are made in consultation with the applicant to ensure that the proposed activities can be carried out either by securing funding through another source and/or modifying the project in accordance with adjusted funding levels and criteria. Such adjustments ensure that allowable maximum funding levels are not exceeded. In the case of the two files cited with lower than required contributions by the sponsor, the MMSB is working with the applicants to make any appropriate, required adjustments. Ongoing monitoring activities will ensure that all disbursements to applicants are in accordance with approved criteria and funding levels.*

##### ***Project Approvals***

*In the case of two applications whereby the Minister's decision was not in line with the Board's recommendation, it should be noted that according to the Waste Management Regulations, final funding approval authority does rest with the Minister. The Board operates only in an advisory capacity through recommendations to the Minister.*



### **3.18 A Review of the Multi-Materials Stewardship Board**

#### ***Board Operations***

##### ***Annual Report***

*While no formal annual report was submitted for the fiscal year 1998-99, information was readily made available to the Minister of Environment and Labour on Board activities throughout the year. Through representation on the Board from the Department of Environment and Labour, there was (and continues to be) ongoing awareness of the Board's activities by the Department. In addition, consistent written correspondence on various issues and operational updates as well as meetings between the Minister of Environment and Labour and the Executive Committee of the MMSB on significant operational issues ensure that the Minister is adequately informed of the Board's operations. A formal annual report will be submitted to the Minister at the end of the 1999-00 fiscal year.*

##### ***Board Remuneration***

*Remuneration paid to any Board member did not exceed the annual limit stipulated by Treasury Board. The function of one Board position requires active involvement in various issues pertaining to the operations of the Board which necessitates a significant time commitment. In future, the claim form presently used will be modified to provide greater detail on the type of work for which payment is being claimed.*

##### ***Adherence to Public Tender Act***

*Up until February 1999, there was significant discussion and legal opinions as to the Board's status and its requirement to adhere to the Public Tender Act. Once this issue was resolved (February 1999) the Board did adhere to the Act. Prior to this clarification on the Board's status, purchase decisions were based on the lowest price of at least three quotations.*

##### ***Travel***

*Three travel claims cited as not properly approved are from very early in the Board's existence. At that time, there was neither permanent staff nor a permanent Chair in place. Once the Board became fully operational with appropriate human resources, a process was established to ensure that all claims were properly approved.*

*The entertainment expense that exceeded Board policy relates to an out-of-town Board meeting. This expenditure was recorded as entertainment in error and should have been posted as a "meeting expense" rather than entertainment.*



### 3.18 A Review of the Multi-Materials Stewardship Board

#### *Conflict of Interest*

*The MMSB has addressed the two possible conflict of interest situations.*

*In one instance, the Board requested a written opinion from the Department of Environment and Labour before carrying out an activity that may have been perceived as a conflict of interest. The Department responded in writing that there was no conflict of interest. It is the MMSB's understanding that prior to providing its opinion, Departmental officials consulted with the appropriate contact for the Conflict of Interest Tribunal and it was determined that this issue did not warrant a formal referral to the Tribunal.*

*The second issue raised in the Auditor General's Report has been referred to the Conflict of Interest Tribunal as recommended. The MMSB is awaiting the Tribunal's opinion on this matter. Based on circumstances surrounding this issue, however, it is felt that the MMSB acted appropriately and that there was no conflict of interest in the matter raised.*

#### **Department's Response**

*It should be noted that the Minister of Industry, Trade and Technology is a member of the Cabinet Committee established to determine the funding allocated to each category of applications for the Trust Fund.*

*With regard to applicants having to provide documentation to confirm their required percentage share of project costs, discussions are held with applicants and final project contributions can be adjusted, if necessary, to reflect such contributions. In any event, the Minister of Environment and Labour has a flexibility to change percentage of required contributions if it is appropriate or necessary to see a desired project undertaken.*

*With regard to the Minister of Environment and Labour's position on the request that refunds be increased to 4¢ and 12¢ for non-alcoholic and alcoholic beverages, respectively, it should be clarified that his position was that, before such an action was undertaken, all other options and their potential impacts on recovery rates should be explored. The current review of the system may provide more direction in this regard.*

*It should be noted that Figure 5 is a **guideline** only for allocating funds. There is no legislated requirement for these allocations and the Minister of Environment and Labour has the ability to vary these allocations based on need and overall government priorities.*

### 3.18 A Review of the Multi-Materials Stewardship Board

*With regard to the Minister approving a project that the Board had not recommended, the insinuation in this declaration could be interpreted as being that the Minister approved something outside of his legislated authority. In the final analysis, all projects approved were consistent with the legislation.*

*With regard to the allocation of the Trust Fund between the various legislated categories, again, it must be stressed that Figure 5 is a guideline only. When the Trust Fund was funded, it was difficult to say what the response would be to any particular funding category. As applications were received, adjustments were made to reflect demands in a particular area and government's overall priority for the fund. The Minister of Environment and Labour has the flexibility to adjust these guidelines as the need arises and does not contravene any legislation by doing so.*

*On the issue of remuneration for one Board Member, government approved the compensation level. It is understood that there is no issue regarding the level of compensation, but rather the method of documentation should be improved and the Board is doing so.*

*On the issue of conforming to the Public Tender Act, there was a debate until February 1999 as to whether or not the Board was obligated to do so. Once it was confirmed that such was the case, the Board has been following the Act.*

*With regard to one of the potential conflict of interest situations, this matter was reviewed by officials of the Department of Environment and Labour and those responsible for Conflict of Interest evaluations. It was concluded that the situation was such that it did not warrant being forwarded to the Conflict of Interest Tribunal.*

*With regard to the other possible conflict of interest situation, while the Department is confident that no conflict of interest situation exists, for certainty, this matter has now been referred to the Conflict of Interest Tribunal.*

### 3.19 Newfoundland Government Sinking Fund

Sinking funds are a pool of cash and investments accumulated by the Government during the life of a debenture, which will be used to pay off that debenture when it matures. Some sinking funds are mandatory because of a requirement outlined in the debenture issue while others are voluntary. The Province has been maintaining sinking funds for many years.

The total amount of cash and investments in the sinking funds varies each year as Government uses cash and investments to retire some debentures while contributing additional cash to sinking funds to repay other debentures.

As at 31 March 1999, the Province had accumulated \$1 billion in its sinking funds which will be used to retire the \$5.6 billion in debenture debt. Figure 1 summarizes the Province's outstanding debenture debt and the related sinking funds over the past five years. The Figure outlines statutory sinking funds and voluntary sinking funds.

**Figure 1**

#### Debenture Debt and Related Sinking Funds 31 March (\$ Billions)

|                                  | 1999             | 1998             | 1997             | 1996             | 1995             |
|----------------------------------|------------------|------------------|------------------|------------------|------------------|
| Debenture Debt                   | 2.8              | 2.8              | 2.7              | 2.8              | 2.6              |
| Statutory<br>Sinking Fund        | <u>.6</u><br>2.2 | <u>.5</u><br>2.3 | <u>.4</u><br>2.3 | <u>.4</u><br>2.4 | <u>.4</u><br>2.2 |
| Debenture Debt                   | 1.1              | 1.0              | 1.3              | 1.4              | 1.5              |
| Voluntary<br>Sinking Fund        | <u>.4</u><br>.7  | <u>.4</u><br>.6  | <u>.5</u><br>.8  | <u>.5</u><br>.9  | <u>.5</u><br>1.0 |
| Debenture Debt - No Sinking Fund | <u>1.7</u>       | <u>1.2</u>       | <u>1.2</u>       | <u>1.4</u>       | <u>1.5</u>       |

#### Summary

|                      | 1999 | 1998 | 1997 | 1996 | 1995 |
|----------------------|------|------|------|------|------|
| Total Debenture Debt | 5.6  | 5.0  | 5.2  | 5.6  | 5.6  |
| Total Sinking Fund   | 1.0  | 0.9  | 0.9  | 0.9  | 0.9  |
| Net Debenture Debt   | 4.6  | 4.1  | 4.3  | 4.7  | 4.7  |

### **3.19 Newfoundland Government Sinking Fund**

In 1994, we made a number of recommendations regarding the Province's sinking funds. While some of our recommendations were implemented, others remain outstanding. The Department of Finance has indicated that they are not in agreement with all of our recommendations.

The Province has sinking funds of approximately \$1 billion in cash and investments and therefore, the recommendations that have not been implemented are still of concern as follows:

- The Province maintains voluntary sinking funds for some of its debentures even though there is no legal requirement to do so. As at 31 March 1999, the Province had \$449 million in its voluntary sinking funds. Government has still not conducted any cost-benefit or other analysis to determine whether it is making optimal use of its cash resources by maintaining \$449 million in its voluntary sinking funds. This raises the issue of whether this is the most efficient use of the government's cash resources since Government must borrow this money.
- The rates at which Government contributes to its sinking funds vary. As a result, in some cases, sinking funds are fully funded before the related debenture becomes due. In these cases, the rate at which the sinking fund is funded could be reduced. This again raises the issue of whether this is the most efficient use of the government's cash resources since Government must borrow this money.
- In many cases, the Province's sinking funds include its own investments. As at 31 March 1999, \$567 million of \$1 billion in sinking fund assets was Province of Newfoundland bonds. As a result, the Province has to pay itself interest on its own bonds which are held in these sinking funds. This situation raises the issue of whether the Province should cancel some or all of its own bonds which are held in the sinking funds to relieve it of interest and principal payments thereby reducing its overall borrowing requirements. Our concern again focuses on whether this is the most efficient use of government's cash resources.

### 3.19 Newfoundland Government Sinking Fund

#### **Recommendations**

*Government should determine whether maintaining voluntary sinking funds of \$449 million is making optimal use of its cash resources. Government should determine whether voluntary sinking funds can be reduced, and if so, to what level. Any decision should be based on a detailed cost-benefit analysis.*

*Government should review its contribution rates to its sinking funds to ensure the accumulation of cash and investments occurs consistently over the life of the related debt.*

*Government should review its policy of maintaining its own debentures as assets in its sinking funds.*

#### **Department's Response**

*The issues covered in this report are similar to those contained in your 1994 Annual Report, and as updated in subsequent Annual Reports.*

*It remains this Department's position that sinking fund contributions essentially represent repayment of debt and the maintenance of sinking funds, whether statutory or voluntary, provides for the orderly redemption of the Province's debenture debt. This avoids large fluctuations in yearly debt redemptions and reduces refinancing exposure. These are important considerations given this Province's relative credit standing.*

*You noted in your 1996 update that the Department of Finance has in fact reviewed the process of setting sinking fund contribution rates. These rates are based upon future value calculations and assumed rates of return and, for voluntary sinking funds, are reviewed periodically and revised so as to prevent the accumulation of significant surpluses. In addition, for all long term debenture issues which have mandatory sinking funds, the Province has the right to review and, if necessary, reduce the sinking fund contribution rates to prevent over-funding. As with the voluntary sinking funds, the contribution rates to those mandatory sinking funds will be reviewed periodically and adjusted as required.*

*With respect to cancelling Province of Newfoundland debentures held in the sinking funds, the position of the Board of Trustees at this time has not changed since 1994. Debentures of the Province held in the sinking funds should not be cancelled until such time as the respective sinking fund becomes fully funded. This is a conservative policy and ensures that the amount of income which the sinking fund earns and can reinvest is increased. The sinking fund grows more quickly and thereby provides greater security for bondholders that funds will be available to redeem their debentures at maturity.*

### **3.19 Newfoundland Government Sinking Fund**

*Most of the Province's voluntary sinking funds were established for the repayment of borrowings from the Canada Pension Plan. As a result of amendments to the Canada Pension Plan, commencing in early 1999 the provinces have been permitted to rollover maturing borrowings for a final twenty year term. If this Province decides to rollover some or all of its maturing Canada Pension Plan borrowings, then the existing sinking funds will not be required for debt retirement. These sinking funds may be cancelled and the monies paid into the Province's Consolidated Revenue Fund. In light of this, the Department will review the practice of maintaining voluntary sinking funds to determine whether such sinking funds can be reduced or eliminated. This review has commenced and should be completed in the coming months.*



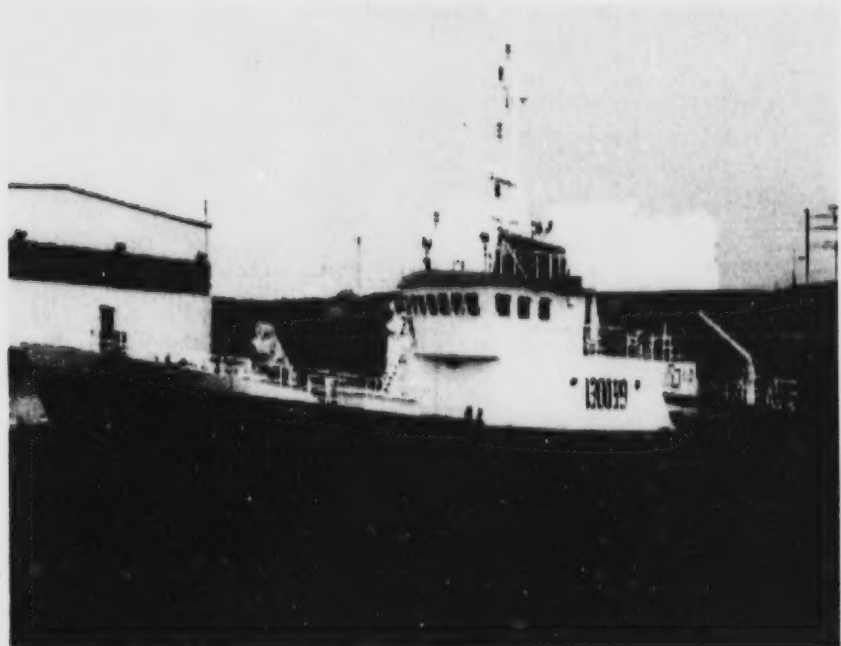
### 3.20 Sale of the Nain Banker

#### Introduction

In my 1997 Annual Report to the House of Assembly, I reported on the four middle distance fishing vessels which had been constructed by the Marystown Shipyard Limited in the 1980's and which were operated by four Corporations created solely for that purpose. The Province has, through senior Government officials, an 85 % ownership interest in these four corporations.

In 1995, three of the four middle distance fishing vessels were sold. The Belle Isle Banker and the Makkovik Banker were sold to Norwegian interests and the Funk Island Banker was sold to local interests. The fourth remaining vessel, the Nain Banker, was leased to the Fisheries and Marine Institute of the Memorial University of Newfoundland. At that time, it was estimated that the total cost of Government's involvement in these four middle distance fishing vessels was approximately \$29.3 million.

In 1997, the Nain Banker was leased to the Torngat Fish Producers Co-operative Society. With the continued operation of the Nain Banker, it was estimated that the total cost of Government's involvement in these four middle distance fishing vessels had increased to \$31.1 million. In 1999, the Nain Banker was sold.



Nain Banker

### 3.20 Sale of the Nain Banker

#### Scope and Objectives

The objective of our examination was to update our 1997 review of the four middle distance fishing vessels and examine the sale of the Nain Banker in March 1999.

#### Conclusions

As at 31 March 1999, the Province's involvement with the four middle distance fishing vessels has cost approximately \$30.7 million.

Under the *Executive Council Act*, assets of the Crown are to be disposed of at the discretion of the individual minister responsible for the management and control of those assets. As a result, there is no requirement that assets be disposed of by public auction or by public proposal call which would give all residents of the Province an opportunity to bid on those assets. However, should assets be disposed of by a public proposal call, all criteria to be used in the selection of the successful bidder should be disclosed to all bidders. This would be similar to the public tender for the acquisition of assets whereby all tender specifications to be used in determining the successful bidder should also be disclosed.

In March 1998, there was a public proposal call for the purchase and/or lease of the Nain Banker. However, in evaluating the proposals, the Board used criteria which was not disclosed in the proposal call and gave preference to bidders who met the undisclosed criteria. Specifically no preference criteria as to where the catch would be landed or where the successful bidder would be based were included as part of the information package accompanying the 1998 request for proposals; however, such criteria were used in awarding the lease.

Three proposals received in 1998, one at \$1.5 million and two at \$1.1 million, resulting from a call for proposals for the sale of the Nain Banker, were eliminated based in part upon financial constraints associated with a required buy-out of the lease obligation. The vessel was sold in March 1999 to another company for \$1 million, only after the referenced lease buy-out had been completed. There was no indication that the three bidders with bids higher than the one accepted were contacted.

#### Detailed Findings

##### 1. Transactions with the Province

The Province's involvement with the four middle distance fishing vessels has cost approximately \$30.7 million as of 31 March 1999. This \$30.7 million is comprised of the amounts outlined in Figure 1.

### 3.20 Sale of the Nain Banker

Figure 1

#### Cost of Province's Involvement with the four Middle Distance Fishing Vessels 31 March 1999

|                                                                                                                                                                      |                       |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------|
| Write-offs relating to the operating advances and lease interest charges for the Belle Isle Banker, the Makkovik Banker, the Funk Island Banker and the Nain Banker. | \$16.7 million        |
| Loss on the sale of the Belle Isle Banker, the Makkovik Banker and the Funk Island Banker.                                                                           | 7.2 million           |
| Operating advances relating to the Nain Banker not yet written off.                                                                                                  | 5.1 million           |
| Lease payout on the Nain Banker.                                                                                                                                     | 2.7 million           |
| Proceeds from sale of the Nain Banker in March 1999.                                                                                                                 | ( 1.0 million)        |
| <b>Estimated Cost</b>                                                                                                                                                | <b>\$30.7 million</b> |

#### 2. Torngat Fish Producers Co-operative Society Limited Lease

At the time of our last review in 1997, the Nain Banker was being leased to the Torngat Fish Producers Co-operative Society Limited. On 6 February 1998, the company gave 30 days notice that it wished to terminate the lease. The middle distance fishing vessel Nain Banker was subsequently returned to St. John's where the Newco IV Corporation took possession of the vessel on 3 April 1998.

In the interim, an invoice in the amount of \$110,232 had been forwarded from the company to the Minister of Fisheries and Aquaculture for reimbursement of expenses incurred during the lease.

On 16 June 1998, a cheque in the amount of \$18,202 was forwarded to the company. The cheque covered the net amount due based upon an estimate of \$34,673 owed for insurance, additional fuel and depreciated cost of the compressor added by the lessee, less \$16,471 in lease deficiencies.

Based upon a review of Board minutes of 21 May 1998, it was the Board's initial position that it was not required under the terms of the lease to reimburse the lessee for certain costs and as a result, these costs were not included in the cheque for \$18,202. A letter was subsequently received from the Minister of Fisheries and Aquaculture asking the Board to reconsider its decision.

On 23 September 1998, the company was advised that the Board had decided to reimburse it for some of these other costs and was paid an additional \$37,500 in January 1999.

### 3.20 Sale of the Nain Banker

#### 3. Request for proposals - Nain Banker

A public proposal call for the purchase and/or lease of the middle distance fishing vessel Nain Banker closed on 13 March 1998. Departmental records indicate that proposals were received from eight bidders. We attempted to determine that all proposals were received within the proper time frame; however, it was not possible to do this as the date was not always indicated on the proposals on file at the Department.

A review of the publicly advertised proposal call and the information package supplied to interested parties indicated that there were no criteria communicated as to any preferences as to where the catch would be landed or where the successful bidder would be based. Figure 2 provides details relating to the proposals received.

**Figure 2**

#### **Lease and/or Purchase Proposals Details of Proposals Received March 1998**

| Proposal | Financial Detail                                                                                                                                                                                                                                                           | Fish Disposition                                           |
|----------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------|
| # 1      | Option A: lease, 15% of gross estimated at \$1,001,000 for 12 months (\$150,150). Option to purchase after 12 months for 1,050,000<br><br>Option B: lease, 15% gross (3-4 months). Option to purchase for \$1,110,000, plus maintenance, insurance, and quadrennial costs. | Labrador plants                                            |
| # 2      | Outright purchase for \$1,500,000                                                                                                                                                                                                                                          | Not specified                                              |
| # 3      | Lease/purchase for 10 annual payments of \$50,000, \$500,000 purchase at end of 10 years, plus maintenance, and quadrennial survey costs.                                                                                                                                  | L'ance au Loup, Labrador and Avalon Peninsula plants       |
| # 4      | Option A: outright purchase for \$1,100,000<br><br>Option B: lease at \$50,000 per year (\$25,000 down and 6 payments for 6 months), plus annual refit, maintenance, insurance, and quadrennial survey costs.                                                              | Tornat Fish Producers, Makkovik, Labrador and Ramea plants |
| # 5      | Lease- in lieu of lease fee (\$50,000), bidder would install freezer capacity and fishing equipment on vessel, plus insurance.                                                                                                                                             | Black Tickle, Labrador plant                               |
| # 6      | Lease for 5 years - \$120,000 annually. Option to purchase for \$800,000 at end of lease, plus refit, maintenance, insurance, and quadrennial survey costs.                                                                                                                | Fogo plant                                                 |
| # 7      | Option A: outright purchase for \$1,100,009<br><br>Option B: lease for 4 years - \$60,000 annually (monthly payments), plus insurance and quadrennial survey costs.                                                                                                        | Not specified                                              |
| # 8      | Outright purchase for \$250,000 (bidder to spend \$200,000 on refrigeration refit)                                                                                                                                                                                         | Nain plant                                                 |

Source: Summary of Proposals prepared by Department of Fisheries and Aquaculture

### 3.20 Sale of the Nain Banker

As indicated in Figure 2, 8 bidders submitted a total of 11 proposals. Our review indicated the following:

- Board minutes dated 31 March 1998 indicated that proposals for purchase of the vessel, including one proposal of \$1.5 million and two for \$1.1 million were eliminated based in part on concerns regarding the buyout of the lease which the Board indicated would require "... a payout by Government of more than \$1.5 million". However, if the Board had concerns over the cost of the buyout of the lease in March 1998, it is difficult to understand why the Board sold the Nain Banker in March 1999 for \$1 million, which was less than bids received a year earlier, and which cost \$2.7 million to buyout the lease; and
- Although not included as a criteria in the public proposal call, proposals indicating the sourcing of Labrador fish plants were given preference over proposals which did not indicate the sourcing of Labrador fish plants.

#### 4. Labrador Fishermen's Union Shrimp Company Limited Lease

On 14 May 1998, Cabinet approved the lease of the Nain Banker to the Labrador Fishermen's Union Shrimp Company. Departmental officials informed us that the Province had established a policy that fish landed in Labrador must be processed in Labrador and the Nain Banker was seen to be suitable for the northern turbot fishery off the coast of Labrador, as well as for use in developmental fisheries efforts.

On 6 June 1998, a lease agreement was signed with the Labrador Fishermen's Union Shrimp Company Limited that provided for the operation of the Nain Banker by the company for a one-year period. The vessel could be used for commercial fishing purposes in Canadian waters only in specified regions, with the vessel's catch to be landed at specified locations in Labrador, where possible. If the operator was unable to land fish at its own plant, then other processing companies in Labrador were to be given the first right of refusal. Neither of these criteria were included in the original proposal call.

The Labrador Fishermen's Union Shrimp Company Limited had the option to renew the agreement for a further year, subject to reaching acceptable terms with the Corporation on the amount of an operating fee, or to negotiate for the purchase of the vessel.

#### 5. Sale of Nain Banker

On 18 March 1999, Cabinet approved the sale of the Nain Banker to the Labrador Fishermen's Union Shrimp Company Limited for \$1 million, and the payout of the lease which was \$2.7 million.



### 3.20 Sale of the Nain Banker

#### Department's Response

- (1) *With respect to the comment that all of the criteria for evaluating a call for public proposals for the lease and/or purchase of the Nain Banker in March, 1998 were not included in the proposal, the following points are made:*
- (i) *that the Board of Directors of the Newco IV Corporation, on behalf of Government, made no decision to sell the Nain Banker in 1998. Rather, a decision, with Government's approval, was made to lease the vessel in 1998 following a review of all proposals submitted in response to the March, 1998 proposal call;*
  - (ii) *A lease/operating agreement for the Nain Banker was entered into shortly thereafter in 1998 between Newco IV Corporation and the Labrador Fishermen's Union Shrimp Company Limited (LFUSC);*
  - (iii) *that under the terms of the 1998 proposal call, all prospective operators/lessees were required to provide a comprehensive fishing plan with their proposal for consideration; all proposals were received within the required deadline;*
  - (iv) *the 1998 lease with LFUSC contained a condition giving the Company an option to negotiate the purchase of the vessel on the basis of a proposal that was acceptable to Newco IV Corporation and the provincial government;*
  - (v) *that based upon an evaluation of the respective fishing plans submitted and of the other elements of each proposal received, the Newco IV Board of Directors on the advice of the Department of Fisheries and Aquaculture decided to accept the company's lease proposal as being the one that best provided for the operation of the vessel in the context of achieving a major policy objective of the Government of Newfoundland and Labrador, in ensuring that appropriate harvesting capacity, i.e. the Nain Banker, would be available to land fish from adjacent Labrador waters for processing onshore in Labrador;*
  - (vi) *that in response to an offer to purchase made to Newco IV Corporation in December, 1998, through the Department of Fisheries and Aquaculture, the Board of Directors of Newco IV Corporation in consultation with its major shareholder, the Government of Newfoundland and*



### 3.20 Sale of the Nain Banker

*Labrador, made a decision, in March, 1999 to sell the Nain Banker to the LFUSC, which sale transaction was also approved by Government and finalized; and*

- (vii) the decision to sell the vessel in 1999 was not made in response to the 1998 call for proposals and there was no legal requirement on Newco IV Corporation or Government to make a subsequent call for proposals.*
- (2) With respect to the decision of Newco IV Corporation to approve the payment of the sum of \$37,500 to Torngat Fish Producers Co-operative Society Limited arising from the Nain Banker lease agreement of 1997 the following points are made:*
  - (i) this decision was made in response to a request from the Company;*
  - (ii) the payment was approved by the Board of Directors of Newco IV Corporation after it had received certain information requested from the engineering and naval architectural staff of the Department of Fisheries and Aquaculture. This information confirmed that a major rebuilding of the main engine of the vessel Nain Banker was completed at Torngat's cost in the aftermath of a major engine malfunction in 1997 while the vessel was leased to Torngat. This expenditure resulted in a real and tangible benefit of dollar value to the amount of \$37,500 in terms of the extension of the period of time the vessel would be able to continue to operate without a further quadrennial survey and refit as a result of the same; and*
  - (iii) this additional amount, in short, was paid out in a prudent business-like manner in exchange for the real and tangible benefits to Newco IV Corporation referred to above.*

### **3.21 Belleoram Scallop Hatchery**

#### **Introduction**

In 1995, Cabinet approved the redevelopment of the former provincial fish plant in Belleoram into a scallop hatchery. This initiative was based on a need for scallop spat (seed) to promote scallop development in the Province, as recommended by the Department. The intent, as stated in the Cabinet approval, was to establish the hatchery but to privatize it as soon as possible. We recommended in our 1998 report item that the Department should comply with Cabinet's direction with regard to the operations of the Belleoram scallop hatchery.

In our 1998 report item, it was indicated that as at 31 March 1998, a total of \$1.5 million had been spent in capital and operating costs relating to the hatchery. Essentially all of this funding was provided either by Government directly or through Federal/Provincial agreements. The amount of investment had increased to \$1.8 million as at 31 March 1999.

A review of information maintained at the Department at the time of our 1998 review indicated that net sales totalled \$5,000 and that production targets were expected to be 7.5 million spat for 1995, the first year of operation and 15 million spat in 1996, the second year. Actual production was approximately 3 million spat in 1995 and was similarly low for 1996. As part of our update review, we determined that production had increased to 5 million spat for 1998; however, this is still less than the original estimated production capacity of 15 million.

#### **Scope and Objectives**

The objective of our review for this year's report item was to determine what action the Department had taken with respect to the redevelopment of the former provincial fish plant in Belleoram.

#### **Detailed Findings**

Although in 1995, Cabinet directed that the hatchery should be privatized as soon as possible, this has not been done to date. Cabinet ordered that after the first year of operation, a report be made on the options and feasibility of attracting the private sector to assume operations of the hatchery. The Department indicated that this report was never made to Cabinet. We recommended in our 1998 report item that the Department should comply with Cabinet's direction with regard to the operations of the Belleoram scallop hatchery.

In our 1998 report item, it was indicated that as at 31 March 1998, a total of \$1.5 million had been spent in capital and operating costs. The amount of investment had increased to \$1.8 million as at 31 March 1999.

### 3.21 Belleoram Scallop Hatchery

A review of information maintained at the Department at the time of our 1998 review indicated that net sales totaled \$5,000 and that production targets were expected to be 7.5 million spat for 1995, the first year of operation and 15 million spat in 1996, the second year. Actual production was approximately 3 million spat in 1995 and was similarly low for 1996. Documentation supporting the low production rate indicated there were overwintering problems due to the late start of production in 1995 and also due to the small size of the spat in relation to expectations. In 1997, there were further production problems due to a major problem with larvae mortality rates in the 80% range. At the time of our 1998 review, discussions with Department officials indicated that production levels were expected to increase substantially during 1998. As part of our update review, we determined that production had increased to 5 million spat; however, this is still less than the original estimated production capacity of 15 million.

In their response to our 1998 report, the Department indicated that the transfer of the scallop research and development program from Memorial University to Belleoram was undertaken on the basis of encouraging results achieved at the Ocean Sciences Centre prior to 1995. It was Government's intention to privatize the Belleoram operation as quickly as possible but initial results were not as promising as those anticipated. This was addressed in the Department's ongoing budget planning process and consequently a specific recommendation to Cabinet recommending privatization was not made. Given the highly technical scientific process associated with this project the Department considered the final project cost to be most reasonable albeit it was higher than the initial estimated cost. It was further indicated that the project had met with most encouraging results in 1998 and that a full report on the future of the operation would be presented to Government in 1999. As well, the success of this facility would have a positive impact on the expansion of the scallop industry.

At the time of our review in relation to this year's report item, the Department indicated that Cabinet had been updated on the situation with the hatchery and that support had been expressed to attract a private sector company to buy or lease the facility.

The Department also provided that while production of seed for 1999 was expected to total approximately 5 million, the provincial seed requirement for the next two to three years is likely to be 2 to 3 million. It is noted that the production capacity of the hatchery was estimated at 15 million annually. In addition, at a 5 million production level, and at an average sales price of \$0.035 per seed proposed by the Department, annual gross revenue would be only \$175,000. The annual operating budget for the hatchery is higher than this amount, which would likely result in deficits.

### 3.21 Belleoram Scallop Hatchery

On 19 May 1999, the Department's Assistant Deputy Minister wrote the hatchery manager indicating that it was the Department's "...intention to provide funding for operation of the hatchery through one more production cycle, specifically to September 30, 1999." It was also indicated that funding would be to a maximum of \$160,000 less revenues from sales. It was further outlined that the Department would start to prepare a divestiture plan.

On 20 May 1999, one day after the date of the above letter from the Assistant Deputy Minister, the Minister wrote the hatchery managers indicating it was the Department's "...desire to extend the existing contract to July 31, 1999 and we seek your agreement." In this letter, it was indicated that the Department was working to secure funding for the operation of the hatchery up to 30 September.

In July 1999, the Department prepared a Divestiture Information Package relating to the proposed sale of the hatchery. The Department indicated that it was decided later not to release the package.

In the same month a report was prepared by the Department's Aquaculture Branch. In the report, it was proposed to continue financial support for the 1999/2000 year and to develop a plan to privatize the Belleoram Hatchery by April 2000.

#### Department's Response

- (1) *With respect to your comment that "on 19 May 1999, the Department's Assistant Deputy Minister wrote the hatchery Manager indicating that it was the Department's intention to provide funding for operation of the hatchery through one more production cycle, specifically to September 30, 1999", the following points are made:*
  - (i) *This incremental funding was made available through the Federal/Provincial, 80%/20% cost shared agreement of ACERA (Aquaculture Component of the Economic Agreement); and*
  - (ii) *The Department concluded that by continuing the operation of the scallop hatchery for the 1999 production season and, provided that the hatchery could duplicate and/or improve upon the 1998 spat survival results, it would be easier to attract a private sector company to buy or lease the facility.*

### 3.21 Belleoram Scallop Hatchery

- (2) *With respect to your comment that in July 1999 the Department prepared a Divestiture Information Package relating to the proposed sale of the hatchery and that the Department indicated that it later decided not to release the package, the following points are made:*
- (i) *This package was not released at that time because of a request made by Coast of Bays Regional Economic Development Board to Ministers Efford and Langdon requesting a 3-6 month delay in its release so that it would be given a sufficient time frame to prepare its own proposal for the future operation of the hatchery under the guidance of the zonal board;*
  - (ii) *Since ACERA had agreed to provide funding to the operation for the 1999 production season then there would be no further financing required by the Province; and*
  - (iii) *It was anticipated that if the Coast of Bays Regional Economic Development Board proposal was not acceptable then a call for proposals for the privatization of the facility could be made within 60 days of receipt of their proposal.*



## **3.22 Sale of Assets**

### **Introduction**

The Department of Fisheries and Aquaculture has a primary mandate to promote the ongoing development of marine fisheries and the aquaculture industry in the Province. Over the years, the Department has made a significant investment in infrastructure in relation to this mandate, through the construction or acquisition of various fisheries related facilities. In recent years, the Department has continued its divestiture effort relating to many of these facilities.

Information provided by the Department indicates that in excess of three hundred major assets have been subject to the divestiture process, with in excess of one hundred assets remaining under Government ownership. Assets subject to divestiture included marine service centres, fish plants, middle distance fishing vessels, community stages, bait sheds and slipways. Assets such as community stages, bait sheds and slipways were in most instances transferred for nominal amounts to local community groups. Two major categories of assets which sold for amounts other than nominal value are marine service centres and fish plants.

### **Marine Service Centres**

Commencing in the 1970's, Marine Service Centres (MSCs) were constructed by the Department under Federal/Provincial funding agreements. The facilities were constructed primarily to service fishing vessels in their respective areas, offering services which included vessel haulout and launching, storage, and equipment rentals. These facilities were initially operated by the Province.

In March 1992, Government adopted a policy whereby certain Government-owned MSCs would be privatized by entering into leasing arrangements with various private groups to operate the centres. Under the agreements, the Department remained responsible for maintaining and upgrading the facilities.

In January 1997, Government decided to divest itself of MSCs. There were 23 MSCs subject to the divestiture process.

### **Fish Plants**

In May 1990, Government decided to implement a program to divest itself of fish processing facilities. There were 66 fish plants subject to the divestiture process.



### **3.22 Sale of Assets**

#### **Scope and Objectives**

We completed our review of the divestiture of marine service centres and fish plants in April 1999.

The objective of our review was to identify the policies developed relating to the various divestiture efforts at the Department of Fisheries and Aquaculture and to assess the procedures followed by the Department in the divestiture process. Our review of MSCs and fish plants included a determination of whether:

- sufficient and appropriate information was available to ensure informed decisions were made during the divestiture process; and
- the Department had the necessary approval to divest itself of assets identified for review.

We examined recent divestiture efforts related to a sample of MSCs and fish plants. Of the 23 Marine Service Centres owned by the Department, we examined sales of the 5 for which agreements had been concluded at the time of our review. The divestiture of the remaining 18 centres was not completed. Of the 66 fish plants owned by the Department in 1990, we examined 5 of the 60 for which agreements had been completed. These 5 were the most recently concluded agreements. The divestiture of the remaining 6 was not completed.

#### **Conclusions**

##### **Marine Service Centres**

Specific direction and terms of reference for the divestiture of Marine Service Centres were established by the Lieutenant-Governor in Council in January 1997. The divestiture process provided that the incumbent lessees were to be given the option of making an offer to the Department of Fisheries and Aquaculture for the purchase of the respective Marine Service Centre. Four of the five Marine Service Centres reviewed were sold to incumbent lessees at negotiated prices. The fifth Marine Service Centre was sold as a result of a public request for proposals. In the five cases reviewed, the Department of Fisheries and Aquaculture generally complied with the direction provided by the Lieutenant-Governor in Council. In all cases, the sales price was significantly less than the appraised values and the capital cost as recorded by the Department.

For the four MSCs sold to the incumbent lessees at negotiated prices, departmental officials indicated that an acceptable price was based upon the judgment of the Government's Divestiture Committee and the particular circumstances surrounding the facility. If Government had called public proposals with the condition that the lessees had the first right of refusal, an acceptable price could have been established through a public proposal call which could have been used as a minimum acceptable offer in negotiations with the current lessee.

## **3.22 Sale of Assets**

### **Fish Plants**

Specific direction and terms of reference for the divestiture of the fish plants were established by the Lieutenant-Governor in Council in May 1990. The divestiture process provided that the incumbent lessees were to be given the option of making an offer to the Department of Fisheries and Aquaculture for the purchase of the respective fish plants. If a negotiated price with the lessees could not be reached, the Department of Fisheries and Aquaculture was to call a public proposal for the sale of the fish plant. The five fish plants reviewed were vacant; therefore, there was a requirement for a public proposal call. Four of the five fish plants reviewed were sold as a result of a public proposal call and accordingly complied with the direction of the Lieutenant-Governor in Council. Amounts received by the Department of Fisheries and Aquaculture for the five fish plants were significantly lower than appraised values.

### **The Lawn Fish Plant**

The fish plant in Lawn was sold to an unsolicited bidder without the benefit of a public proposal call. As a result, this sale did not comply with the direction of the Lieutenant-Governor in Council which required a public proposal call. In addition, a review of departmental files disclosed that six other unsolicited expressions of interest had been received prior to the sale of the Lawn fish plant.

Authorization by the Lieutenant-Governor in Council for the sale of the Lawn fish plant included a requirement that the Department of Fisheries and Aquaculture receive a written commitment from the buyer regarding capital investment and employment levels. A letter was received from the purchaser indicating plans for investment of \$300,000 over five years and disclosing the current average weekly employment level; however, sale documents did not include any commitment as a condition of the sale. An official of the Department indicated that there has been no follow-up to determine the amount of capital investment to date or the recent employment history of the fish plant at Lawn.

### **3.22 Sale of Assets**

#### **Findings and Recommendations**

##### **Marine Service Centres**

The divestiture of MSCs was to be carried out in accordance with guidelines approved by the Lieutenant-Governor in Council and included the following:

- incumbent lessees, during the term of their existing lease, were to be given the option to purchase the facility outright or to enter into a lease purchase agreement;
- vacated centres were to be advertised for sale or lease;
- unsold facilities could be offered to community-based organizations;
- each divestiture was to be conducted in accordance with a detailed Terms of Reference which provided further guidance to the Department on the process, including a requirement for one independent appraisal;
- each individual divestiture proposal was to be subject to approval by the Lieutenant-Governor in Council; and
- a communications plan was to be prepared for the initiative.

At the commencement of our review, there had been three MSCs sold outright and two lease/purchase agreements concluded, as part of the current divestiture process. Departmental officials indicated that they had been close to signing a number of additional agreements. We selected the five sales and lease/purchase agreements which had been concluded at that time for testing. The results are as follows.

#### **1. Financial analysis**

Our review of the five agreements selected indicated that the sales prices were found to be significantly less than appraised values for the facilities and in many cases were not much higher than the appraised land value. In addition, the sales prices were well below the capital investment the Department had made in the facilities. In the case of the Burgeo MSC, the site was actually sold for significantly lower than the appraised vacant land value of the site. Financial information relating to the centres reviewed is shown in Figure 1.

### 3.22 Sale of Assets

Figure 1

#### Marine Service Centres Reviewed Financial Information

| Marine Service Centre  | Capital cost              | Appraised land value (if vacant) | Total appraised value     | Agreement Date | Sale price              | Sale price as a % of total appraised value |
|------------------------|---------------------------|----------------------------------|---------------------------|----------------|-------------------------|--------------------------------------------|
| Harbour Grace (Note 1) | \$3,769,517               | \$132,000                        | \$631,000                 | April 1998     | \$200,000               | 31.7%                                      |
| Old Perlican           | 1,126,080                 | 52,100                           | 185,350                   | Aug. 1998      | 90,000                  | 48.6%                                      |
| Burgeo (Note 2)        | 85,344                    | 30,000                           | 67,000                    | Sept. 1998     | 13,400                  | 20.0%                                      |
| Fermeuse (Note 3)      | 2,700,000                 | 72,200                           | 251,200                   | Oct. 1998      | 125,000                 | 49.8%                                      |
| Hodge's Cove           | <u>2,200,000</u>          | <u>28,500</u>                    | <u>130,000</u>            | Nov. 1998      | <u>42,500</u>           | 32.7%                                      |
| <b>Total</b>           | <b><u>\$9,880,941</u></b> | <b><u>\$314,800</u></b>          | <b><u>\$1,264,550</u></b> |                | <b><u>\$470,900</u></b> | <b>37.2%</b>                               |

Source: Department of Fisheries and Aquaculture

Note 1: lease/purchase over a 15 year term

Note 2: sold through public request for proposals

Note 3: lease/purchase over a 12 year term

## 2. Divestiture process

As indicated previously, specific direction and terms of reference for the divestiture process were established by the Lieutenant-Governor in Council. The divestiture approach provided that the incumbent lessees were to be given the option of making an offer to the Department of Fisheries and Aquaculture for the purchase of the respective MSC. A MSC Divestiture Committee, comprising representatives from the Department of Fisheries and Aquaculture, the Department of Finance and the Department of Justice was to make initial decisions on sales negotiations. Upon acceptance by the Committee, the Minister of Fisheries and Aquaculture reviewed each sale and the Lieutenant-Governor in Council gave final approval. After obtaining this approval, legal documents were to be prepared and signed by the parties involved to finalize the sale.

### 3.22 Sale of Assets

Each individual sale reviewed began with the receipt of an initial purchase offer from the incumbent lessee. Typically, the initial offer was not accepted and a counter offer was made by the Divestiture Committee. Negotiations would continue until there was an offer acceptable to the Committee. Minutes of the Committee provided information such as the receipt of offers, decisions of the Committee, counter proposals, and other required actions; however, the rationale for specific decisions such as an acceptable sale price was not documented in the minutes. A Departmental official indicated that an acceptable price was based upon the judgement of the Committee and the particular circumstances surrounding the facility.

An agreement was not finalized with the operator of the Burgeo MSC. This centre was subsequently sold through a public request for proposals. In this instance, only one offer was received.



Marine Service Centre at Hodges Cove with Straddle Crane in foreground

The evaluation criteria developed and used by the Divestiture Committee consisted of a number of identified factors which were to be considered in evaluating a proposal. They included a requirement whereby a rationale was to be provided as to why the facility should be sold at a price less than appraised value. In the case of all MSCs, the cost of continuing to operate the centre was determined to be greater than the revenues which could be generated if it remained Government-owned.

In its most recent Marine Service Centre Annual Report, relating to the 1994-95 fiscal year, the Department indicated that costs to operate the centres in that year totalled \$2.2 million, while total revenues totalled \$0.8 million.

Although, this would appear to be the financial rationale for each sale, it did not assist in determining what would be considered an acceptable sales



### **3.22 Sale of Assets**

price. This is particularly important in that in four of five instances reviewed, the existing lessee used their option to make a purchase offer. Consequently, in those instances, there was no request for public proposals. Had such a request for proposals been conducted, the Department would have been provided with additional information to support an acceptable sales price, which could have been presented to the incumbent lessee for acceptance or rejection relative to the purchase option.

All five sales of the Marine Service Centres were approved by the Lieutenant-Governor in Council.

#### **3. Communication plan**

As part of the divestiture process for MSCs, the Lieutenant-Governor in Council directed the Department to prepare a communication plan for the initiative, in consultation with the Executive Council Secretariat. An official of the Department indicated that this direction was acted upon and that a formal communication plan was prepared.

#### **4. Continuation of MSC services**

Sale agreements in place do not provide for the continued use of MSCs as launch/haulout facilities. There is a provision in the sales agreements which requires the purchaser to maintain the straddle crane needed to provide such services on the site, for five years. If the operator were to cease maintaining the crane during the period, the specified remedy for the Department would be to regain title to the crane. Beyond the five-year period, there is no obligation related to site operation for the purchaser. Consequently, there is a risk that local area users may not be provided with marine services at these centres in the future. The continued provision of marine services has been raised as a concern in meetings held by the Department with local groups.

#### **5. Appraisals methods**

Not all appraisal valuation methods directed to be utilized by the Lieutenant-Governor in Council were used in appraisal estimates obtained by the Department. The appraisers found that due to a lack of comparable sales information and the low rental values used by the Department, only a cost based approach was applicable in the circumstances.

#### **6. Accounts Receivable**

The following instances were identified where lease payments related to MSC operations were found to be in arrears.



### **3.22 Sale of Assets**

- **Harbour Grace MSC**

The repayment schedule for the Harbour Grace lease/purchase agreement included an amount of \$26,175 for past lease fee arrears. This amount was financed by the Department in combination with the \$200,000 sales price to arrive at a principal balance of \$226,175, which was required to be repaid over the 15 year term of the lease/purchase agreement. The first payment of \$24,784 was made at the time the agreement was signed. However, as of April 1999, arrears of lease payments totalled \$30,877. An official of the Department indicated that contact had been made with the lessee in an attempt to recover the arrears. Subsequent to our review, we were advised that this arrears amount had been recovered.

- **Hodges Cove MSC**

At the time of the sale of the Hodges Cove MSC, the incumbent lessee owed an outstanding balance of \$1,342 related to arrears on prior lease fee payments. Due to an oversight at the Department, the amount was not recovered as part of the sale process. The Department advised that efforts would be made to recover the amount. Subsequent to our review, we were advised that the amount had been recovered.

#### **7. Transitional fee structure**

The Lieutenant-Governor in Council directed that consideration be given to a transitional fee structure with prospective owners. This was intended to eliminate the possibility of the private sector operators significantly increasing the former price structure. The Department did consider a transitional fee structure as directed and decided to lift the restrictions on fees charged by existing MSC operators.

#### **8. Right of first refusal provisions**

Included in documentation related to the sale of the Burgeo MSC was a right of first refusal agreement. The agreement contained a clause which, in the event of a proposed sale, would allow the Province to purchase the MSC assets for the lesser of the proposed sale amount and \$125,000. Upon discussion with Department officials, it was determined that the amount indicated in the agreement was in error. The amount indicated should have been the sale price of \$13,400 for the Burgeo MSC and not the amount of \$125,000 indicated. This clause, if uncorrected, could have resulted in the Province having to buy back the MSC for \$111,600 in excess of what was intended.

### **3.22 Sale of Assets**

An official of the Department indicated that a Deed of Rectification would be prepared and signed by both parties to the agreement to correct the error. Subsequent to our review, we were advised that the Deed of Rectification had been prepared and arrangements were being made for signing.

#### **Fish Plants**

The divestiture of fish processing facilities was to be carried out in accordance with guidelines approved by the Lieutenant-Governor in Council and included the following:

- two independent appraisals were to be submitted where facilities were being purchased by the current operator;
- each individual divestiture proposal was to be approved by the Lieutenant-Governor in Council; and
- the Department was to submit progress reports on the divestiture program to the Lieutenant-Governor in Council on a semi-annual basis.

In addition, terms of reference were established by the Lieutenant-Governor in Council which included provisions whereby:

- divestiture of facilities should be for their best demonstrated use and in accordance with other government policy;
- incumbent lessees, during the term of their existing lease, were to be given the option to purchase the facility outright or to enter into a lease purchase agreement; and
- in instances where negotiations could not be concluded the facilities were to be advertised for sale or lease.

We selected the five most recently concluded divestiture agreements for review. The results are as follows.

#### **1. Financial analysis**

Sales values were found to be low in relation to appraised values for the facilities. Financial information related to the fish plants is included in Figure 2.

### 3.22 Sale of Assets

Figure 2

#### Fish Plants Reviewed Financial Information

| Fish plant     | Independent Appraisal Date | Appraised land value (if vacant) | Total appraised value   | Sale date                 | Sale price              | Sale price as a % of total appraised value |
|----------------|----------------------------|----------------------------------|-------------------------|---------------------------|-------------------------|--------------------------------------------|
| Parson's Pond  | Dec. 1993                  | \$ 3,500                         | \$ 65,000               | Aug. 1996                 | \$ 18,692               | 28.8%                                      |
| St. Lawrence   | Aug. 1992*                 | 31,000                           | 400,000                 | March 1997                | 250,000                 | 62.5%                                      |
| Branch         | Nov. 1991                  | 5,000                            | 76,000                  | July 1997                 | 5,001                   | 6.6%                                       |
| Lawn           | Oct. 1993                  | 1,640                            | 65,000                  | Oct. 1998                 | 1                       | 0.0%                                       |
| Change Islands | Feb. 1997                  | 500                              | 90,000                  | Agreement to be finalized | 1                       | 0.0%                                       |
| <b>Total</b>   |                            | <b><u>\$41,640</u></b>           | <b><u>\$696,000</u></b> |                           | <b><u>\$273,695</u></b> | <b>39.3%</b>                               |

Source: Department of Fisheries and Aquaculture

\*- appraisal adjusted internally by Departmental staff to \$321,415

## 2. Divestiture process

As indicated previously, specific guidelines and terms of reference for the fish plant divestiture process were set by the Lieutenant-Governor in Council. The divestiture approach, as directed by the Lieutenant-Governor in Council, provided that the incumbent lessees were to be given the option of making an offer to purchase the facility. If the fish plant could not be sold to the incumbent lessee, the Lieutenant-Governor in Council directed that the fish plant be sold through a public proposal call. A Plant Divestiture Committee, comprising representatives from the Department of Fisheries and Aquaculture, the Department of Finance and the Department of Justice made initial decisions on negotiations for the sale of the fish plants.

All five fish plants reviewed were vacant at the time each of the individual divestitures commenced. In four of the five cases, the fish plant was sold as a result of a public proposal call. In these four cases, the fish plant was sold to the highest bidder. However, in the case of the Lawn fish plant, there was no request for public proposals as required by the Lieutenant-Governor in Council.

### **3.22 Sale of Assets**

The latest meeting of the Plant Divestiture Committee was on 26 March 1996. A departmental official indicated that the Committee has not met since that date. This Committee, which was set up to advise on the fish plant divestiture program did not review the sale of two of the five fish plants that we reviewed. In these two instances, the sales were reviewed by, and initial recommendations made by, officials of the Department of Fisheries and Aquaculture. The Minister of Fisheries and Aquaculture reviewed each sale and the Lieutenant-Governor in Council approved each individual sale. After obtaining this approval, legal documents were to be prepared and signed by the parties involved to finalize the sale.

#### **3. Findings Related to Individual Fish Plants**

In addition to general observations made on the fish plant divestiture process, the following comments are related to individual fish plants.

##### **Lawn fish plant**

The fish plant at Lawn was sold to a private company for a nominal amount. The sale was based upon an unsolicited proposal received from the company. Authorization by the Lieutenant-Governor in Council for the sale of the Lawn fish plant included a requirement that the Department of Fisheries and Aquaculture receive a written commitment from the buyer regarding capital investment and employment levels. A letter was received from the purchaser indicating plans for investment of \$300,000 over five years and disclosing the current average weekly employment level; however, sale documents did not include any commitment as a condition of the sale. An official of the Department indicated that there has been no follow-up to determine the amount of capital investment to date or the recent employment history of the fish plant at Lawn.

There was no public proposal call for the sale of the Lawn fish plant as required by the Lieutenant-Governor in Council. In addition, a review of departmental files disclosed that six other unsolicited expressions of interest had been received prior to the sale of the Lawn fish plant.

##### **St. Lawrence fish plant**

The St. Lawrence fish plant was sold for \$250,000 in March 1997 as a result of a public proposal call. Under the terms of the sale, a \$50,000 payment was made at the time of the sale with the remaining balance of \$200,000 due by 31 December 1997. The interest rate on the outstanding balance was equivalent to the prime rate of borrowing plus 2 percent. The purchaser did not pay the remaining balance of \$200,000 by 31 December 1997, as required by the sales agreement. In September 1998, officials of the Department renegotiated the terms of agreement whereby repayment of the \$200,000 was to be made by five annual payments of \$40,000

### 3.22 Sale of Assets

commencing on 18 April 1998. In addition, interest would be charged at a reduced interest rate equivalent to the prime rate of borrowing. As of the date of our review, the principal payments had been received according to the terms of the subsequent agreement; however, the Department had not received related interest payments.

#### Recommendations

*In order to ensure the maximum benefit is received by the Province from the sale of assets, a public tender offering should be considered as part of the process. Such a public tendering offering would assist applicable divestiture committees in determining what constitutes an acceptable sale price for assets subject to divestiture.*

*The Department should comply with guidelines and terms of reference established by the Lieutenant-Governor in Council.*

*The Department should review and follow-up outstanding accounts receivable balances related to Government-owned assets.*

#### Department's Response

1. *Under the section entitled Marine Service Centres, it is stated that "if Government had called public proposals with the condition that the lessees had the first right of refusal, an acceptable price could have been established through a public proposal call which could have been used as a minimum acceptable offer in negotiations with the current lessee."*

*Initially, Government undertook a public call for proposals to determine the private sector's interest in leasing these properties, with the clear understanding that they would be maintained and enhanced as marine support facilities. In most cases, the companies that leased these centres either brought already established businesses to the sites or undertook major investments in the enhancement/expansion of existing marine services. When the decision was made to pursue the divestiture of the properties, Government made it very clear that many factors would be considered beyond just the actual price received. In this regard, the lessees' overall investment to date, as well as projected future investment, were major considerations. The objective was to ensure that the sites continued as marine support facilities. Furthermore, Government felt that it was not unreasonable to initially deal with the existing lessees who, for the most part, had already undertaken significant investment in these businesses. It was nevertheless clearly understood by all parties that the option*



### 3.22 Sale of Assets

to publicly call for proposals was a consideration should negotiations fail.

2. *With regard to the sale of fish plants, your report stated that the amounts received by the Department of Fisheries and Aquaculture for the five (5) fish plants studied were significantly lower than the appraised values.*

*While this may be true, there were nevertheless many factors considered, with the price being just one consideration. The history of the operator, as well as the future business plans and proposed investments, were also major considerations and very important from an overall economic development perspective.*

3. *With regard to the sale of the Lawn fish plant, your report noted that there was no public call for proposals and stated that this sale did not comply with the direction of the Lieutenant-Governor in Council which required a public proposal call.*

*The Department notes that under the Executive Council Act, the legal authority for the divestiture of all such assets rests with the Minister of Fisheries and Aquaculture. In this regard, the Minister made the decision to divest of this property and sought, and obtained, approval from the Cabinet before doing so.*

4. *Your review expressed concern that the sale documents relating to the Lawn fish plant did not include any commitment relating to the purchaser's capital investment and employment levels. While a letter was received from the purchaser indicating plans for the investment of \$300,000 over five (5) years, your review stated that this should have been included in the sale document.*

*The Order-in-Council which authorized this sale indicated that such terms and conditions were to be developed as either the Departments of Fisheries and Aquaculture or Justice may require. No specific direction was given with regard to the above being included in the sale documents. The Department felt at the time, and still believes, that the letter provided by the purchaser adequately fulfilled the requirement and direction as ordered in OC '98-213. Departmental staff have ready access to the plant and have confirmed that a considerable investment has already been completed by the purchaser on the rehabilitation and modernization of the property. Furthermore, the sale of this facility is considered very current, having a registration date of January 12, 1999. Additional follow-up will therefore be*



### 3.22 Sale of Assets

*undertaken over the coming months as an integral part of an ongoing review process.*

*The following comments also apply with regard to the recommendations. In this section, it is recommended that:*

- a. A public tender offering should be considered as part of the divestiture process;*
- b. The Department should comply with guidelines and terms of reference established by the Lieutenant-Governor in Council;*
- c. The Department should review and follow up outstanding accounts receivable balances related to Government-owned assets.*

*In response to the recommendation that a public tendering offering would ensure that the maximum benefit is received by the Province from the sale of assets, it is maintained that there are many factors to be considered when ensuring that the maximum benefit is received. While the actual price received for the asset is important, there are other issues that are considered equally important. Issues such as the track record of the purchaser, the stability and financial position of the company and its future business plans are critical elements that were major considerations of the divestiture of assets process.*

*Compliance with the guidelines and terms of reference, as established by the Lieutenant-Governor in Council, were followed to the effect that an MC or OC was issued for the sale of each and every property divested by the Department of Fisheries and Aquaculture. While the process may have varied to some degree with regard to the divestiture procedures, all such sales were approved by Cabinet.*

*With regard to the review and follow-up of outstanding accounts receivables, it can be noted that all such accounts are formally reviewed on a quarterly basis. Follow-up action, where appropriate, is undertaken by Departmental staff in conjunction with the Department of Justice.*

### **3.23 Aquaculture Program**

#### **Introduction**

The Department of Fisheries and Aquaculture has a primary mandate to promote the ongoing development of marine fisheries and the aquaculture industry. Policies and programs have been developed to support this mandate in harvesting, processing and marketing.

Aquaculture means the cultivation of aquatic plants or animals. In Newfoundland, aquaculture activity relates to finfish and shellfish cultivation. Finfish includes such species as steelhead trout, Atlantic salmon, arctic char, cod, and rainbow trout. Shellfish includes such species as blue mussels and scallops.

In my 1998 Annual Report to the House of Assembly, I included an item in part 3.13 relating to my review of the Aquaculture Program.

The review concluded in part that:

- During the year ended 31 March 1998, Government authorized the issuance of a loan guarantee to an aquaculture licensee. As at 31 March 1998, the limit of the loan guarantee was \$5.0 million with a current liability of \$3.85 million. A corresponding provision was included in the Province's financial statements for the year ended 31 March 1998, to reflect the probable loss to be incurred relating to this loan guarantee. In July 1998, Government authorized an increase of the limit for the loan guarantee to \$6.0 million. In September 1998, the Department requested that Cabinet approve a further increase in this loan guarantee to \$6.7 million.

#### **Scope and Objectives**

The objective of our review for this year's report item was to determine what action the Department had taken with respect to the issue raised in the 1998 report item relating to the issuance of a loan guarantee to an aquaculture licensee with a limit as at 31 March 1998 of \$5.0 million, which had been increased to \$6.7 million in September 1998.

#### **Conclusions**

In my 1998 Annual Report I commented on the issuance of a loan guarantee to an aquaculture licensee. Government's involvement with this aquaculture licensee is estimated to have cost the Province a total of \$9.3 million in loans and loan guarantees as of 31 March 1999. Despite the infusion of \$9.3 million from Government, the licensee's financial position has deteriorated significantly.

Of the \$9.3 million, \$2.8 million is owed to Enterprise Newfoundland and Labrador Corporation and \$6.5 million relates to a loan guarantee. Government paid \$5 million of the loan guarantee in March 1999 and

### 3.23 Aquaculture Program

expects to pay the remaining \$1.5 million in 1999-2000. It is unlikely that Government will recover any of the \$9.3 million.

Although Government initially had security in place for these loans and loan guarantees, Government relinquished some of its security in favour of other creditors in an effort to keep the company operational.

#### Detailed Findings      Background information relating to Government involvement

During the 1990's, the aquaculture licensee had significantly expanded its operations. The company operated seven licensed marine growout sites with almost all service requirements being developed internally. Operations included a hatchery, processing plant, feed delivery, and diving services. In 1997, the company approached Government seeking financial assistance. In September 1997, an agreement was signed between Government and the company which provided working capital funding of \$2.6 million in the form of a Government guaranteed bank loan.

As a condition for providing this funding, the Department assumed management responsibility of the company, appointed an Assistant Deputy Minister as interim general manager, and placed two representatives on the company's Board of Directors. Figure 1 outlines the history of Government's loan guarantee limits for the company:

Figure 1

#### Loan Guarantee Limits

| Agreement Date | Amount        |
|----------------|---------------|
| September 1997 | \$2.6 million |
| October 1997   | \$4.0 million |
| March 1998     | \$5.0 million |
| August 1998    | \$6.0 million |
| October 1998   | \$6.7 million |

### 3.23 Aquaculture Program

In addition to Government's loan guarantee, the company owed Enterprise Newfoundland and Labrador Corporation approximately \$2.8 million as at 31 March 1998, including accrued interest.

In July 1998, Cabinet directed the following:

- That the Minister of Fisheries and Aquaculture, in consultation with the Minister of Finance and President of Treasury Board, report back to Cabinet within one month with a plan to include: restructuring the company's finances; eliminating Government's involvement in the aquaculture operations carried out by the company; and facilitating the sale of the operation to an operator with experience in the industry and the means to undertake further needed investments.
- That the company obtain an agreement from its feed supplier not to take action prior to 31 August 1998 to recover debts owed to it by the company.

The company did not obtain an agreement from its feed supplier not to take action prior to 31 August 1998 to recover debts owed to it by the company, rather it was arranged by Government entering into an agreement with the feed supplier to subordinate Government's loan guarantee security, consisting of a first charge on all inventory, including fish and feed inventory. It was indicated that this agreement was required in order to prevent the feed supplier from enforcing its claims on the company, which at the time amounted to approximately \$3.5 million. The original security for the loan guarantees was provided in September 1997, when the Province and the company signed an agreement which gave the Province mortgage security on the company's assets.

In September 1998, the Department requested and Cabinet approved a further increase in this loan guarantee to \$6.7 million.

On 2 March 1999, Cabinet directed that the Minister proceed to transfer the administration and control of the company back to its shareholders, subject to the Ministers of Fisheries and Aquaculture, and Finance agreeing on the terms and conditions of the transfer.

On 3 March 1999, the Minister of Fisheries and Aquaculture proposed to the company that management would be transferred back to the company and Government would pay down the outstanding balance of the loan guarantee, estimated at that time to be \$6.5 million, write off the loan balance with the Enterprise Newfoundland and Labrador Corporation of approximately \$2.8 million, and release the Province's security **subject to** the following conditions being met:

### 3.23 Aquaculture Program

- removal of the Department's Assistant Deputy Minister from his General Manager responsibilities with the company;
- the company's current guaranteed line of credit with its bank be frozen;
- trade payables outstanding at the date of transfer be the responsibility of the company;
- removal of Government representatives from the company's Board of Directors;
- release of the Province's security (first charge on fixed assets and subordinate charge on feed inventory), subject to the company hiring and putting in place a new General Manager, finding a new investor and submitting a viable Business Plan for continued operations acceptable to Government; and
- the company negotiate with the Atlantic Canada Opportunities Agency with respect to related debt.

On 30 March 1999, Government paid \$5 million of the \$6.5 million loan guarantee to the company's bank although not all of the conditions outlined in the Minister's letter were met. For example: the company had not hired a new General Manager; no new investors had been identified; and the company had not completed negotiations with the Atlantic Canada Opportunities Agency with respect to related debt. Furthermore, although a Business Plan for continued operations was submitted before the \$5 million payment was made, it was not acceptable to Government.

In addition, Government indicated that it would pay up to the remaining \$1.5 million after the loan guarantee approvals in excess of \$5 million were ratified by the House of Assembly. The \$5.0 million partial payment has been recorded as a receivable in the Province's financial statements for the year ended 31 March 1999 with a corresponding provision made to reflect the probable loss.

#### **Government Loan Security**

Although Government initially had security in place for the loans and loan guarantees to the company, some of the security was relinquished in an effort to keep the company operational. For example:

- In October 1996, the Enterprise Newfoundland and Labrador Corporation entered into an agreement with the company and its



### **3.23 Aquaculture Program**

feed supplier which subordinated the Corporation's security to debt the company had incurred with the feed supplier.

- In December 1997, two of the company's shareholders signed agreements whereby each would guarantee \$112,500 of Government's loan guarantee in the company. These guarantees were never realized.
- On 11 August 1998, Government entered into an agreement with the company's feed supplier to subordinate Government's loan guarantee security, consisting of a first charge on all inventory, including fish and feed inventory, in order to prevent the feed supplier from enforcing its claims on the company, which at the time amounted to approximately \$3.5 million. The original security for the loan guarantees was provided in September 1997, when the Province and the company signed an agreement which gave the Province mortgage security on the company's assets.
- On 23 August 1999, Government entered into a further agreement to subordinate its security over the company's fish inventory to enable the company to use it as security for another feed supplier.

#### **Financial Condition of the Company**

As at 31 March 1999, the Province had provided a total of approximately \$9.3 million in assistance to the company, relating to the \$6.5 million balance of the \$6.7 million loan guarantee and the outstanding balance of \$2.8 million in loans from the Enterprise Newfoundland and Labrador Corporation. In addition, the Federal Government through the Atlantic Canada Opportunities Agency, had provided \$3.5 million, including \$2.4 million in repayable contributions and loans and \$1.1 million in grants.

Despite the infusion of this funding, the company's financial position has deteriorated significantly. It is unlikely that Government will recover any of the \$9.3 million.

#### **Divestiture efforts**

In October 1998, Cabinet struck a committee of Ministers to evaluate proposals for the divestiture of the company and to report back to Cabinet as appropriate. These proposals had been invited during the summer of 1998, based on a Divestiture Information Package dated 31 July 1998.

The Divestiture Information Package was distributed to 11 companies. Of these 11 companies, only 2 responded with offers.



### 3.23 Aquaculture Program

The first offer was from a company based in the Province. This company offered to assume 100% of the licensee's shares for \$1, to inject \$2 million in capital infrastructure over an 18-24 month period, and to repay existing debt at the rate of \$10,000 per year or 10% of net after tax profit. This offer was subject to Government paying off all existing creditors.

The second offer was from a company based in Nova Scotia. This company offered to pay each shareholder an immediate 25% of share value, estimated at \$250 per share, or 100% of share value after three years, whichever the shareholders agreed to. It also agreed to finance a new blast freezer and other freezing units.

Neither of these divestiture offers were accepted by the licensee or Government. The first offer was rejected by the Board in large part due to the existing shareholders not wanting to sell their shares for \$1.

#### Other Matters

In June 1998, the licensee was advised that certain transactions between it and another related company "...feature prominently" in a bankruptcy petition against the other company. The transactions referred to were "...various fraudulent sales/fraudulent conveyances/fraudulent transfers of the fish inventory and sale proceeds thereof from (the related company) to" the aquaculture licensee. The Department indicated that no action was taken directly against the licensee resulting from this petition.

In March 1999, the Federal Minister of Fisheries and Oceans wrote the Minister of Fisheries and Aquaculture regarding the latter's correspondence concerning the importation of all diploid, all female steelhead trout into the Bay d'Espoir area. In his letter, the Federal Minister confirmed his agreement that such fish could be used for commercial scale trials provided that the fish came from a source approved by the Department of Fisheries and Oceans. As well, in the letter, the Federal Minister reiterated his earlier authorization for the use of diploid Northwest Atlantic salmon stocks in Bay d'Espoir, including commercial scale trials. The previous restrictions relating to the use of such fish stocks were seen by the licensee and Government as a serious threat to the development of aquaculture in the Bay d'Espoir area.

#### Department's Response

- (1) *With respect to your statement that on March 30, 1999, Government paid \$5.0 million of the \$6.5 million loan guarantee to the company's bank although not all of the conditions outlined in the Minister's letter were met, we make the following points:*

### 3.23 Aquaculture Program

- (i) *Writing off of the debt was not conditional on all of these conditions being met (see letter of March 3, 1999); however, release of security was conditional upon (f) of Minister's letter dated March 3, 1999, specifically;*
  - (a) *that the company hires and puts in place a new general manager;*
  - (b) *finds a new investor; and*
  - (c) *submits a viable Business Plan for the continued operations, that is acceptable to Government.*
- (2) *With regards to your comment that despite the infusion of \$9.3 million from Government, the company's financial position has deteriorated significantly, we note in the following points that the deterioration could not be solely stemmed by cash infusion, and other non financial considerations impacted the company as follows:*
  - (i) *The company had reached a point whereby the management skills to move the operation from a research and development mode to commercial viability were not available in-house;*
  - (ii) *Excessive overruns on its capital expansion projects. These overruns were financed from operating capital;*
  - (iii) *Major mortalities on 1997 year class of steelheads due to a parasite;*
  - (iv) *Poor husbandry practices at the hatchery led to severe overcrowding of fish which resulted in severe losses of fish at the hatchery. Due to the overcrowding at the hatchery, fish going to the ocean sites were very small and weak which resulted in unusually high mortalities for both salmon and steelhead in 1997 and 1998;*
  - (v) *Higher than acceptable industry costs for site operations and processing; and*
  - (vi) *Due to DFO regulations the company had to use inferior strains of steelhead (Triploids), which resulted in poor feed conversion ratios and unusually high mortalities during the growout cycle, which placed the company in a non competitive position.*

### 3.23 Aquaculture Program

- (3) *With regards to your statement that it is unlikely that Government will recover any of the \$9.3 million, we make the following points:*
- (i) *Government invested \$9.3 million in loans and loan guarantees into the company in order to allow the industry to move from a Research and Development mode to one [of] commercialization of the overall aquaculture industry in Bay d'Espoir;*
  - (ii) *The continuation of this operation will provide direct employment for 200 persons in an economically depressed, and isolated region of the Province; and*
  - (iii) *Despite a deterioration in the financial performance of the company over this time frame the infusion of cash into the operation will place the company on a more financially stable footing, and will allow the company a better opportunity for survival.*

### **3.24 Legacy Nature Trust**

#### **Introduction**

On 22 March 1999, Government announced in its 1999 Budget Speech the establishment of the Newfoundland and Labrador Legacy Nature Trust. The trust was to be established as a non-profit agency with a mandate to raise funds nationally and internationally to finance conservation projects in Newfoundland and Labrador. In the 1999 Budget Speech Government made a commitment to contribute \$1 million to the trust.

On that same day, the Minister of Forest Resources and Agrifoods provided further information on the Legacy Nature Trust and indicated that the trust would be incorporated and registered as a charitable non-for-profit agency in Canada and the United States. The \$1 million was intended to fund the basic operations of the trust over the first five years or so.

On 12 March 1999, Government issued a special warrant for \$1 million indicating that these funds were urgently required for the Newfoundland and Labrador Legacy Nature Trust. On 31 March 1999, a cheque for \$1 million was issued and recorded as an expenditure in Government's fiscal year ended 31 March 1999, thus increasing Government's expenditures by \$1 million and reducing Government's cash by \$1 million.

#### **Findings**

Our review indicated numerous concerns regarding the issuance of this \$1 million cheque:

- Although Government indicated that the \$1 million was urgently required on 12 March 1999, the cheque was not issued until 31 March 1999. At that time, the Newfoundland and Labrador Legacy Nature Trust did not exist. In fact, the Newfoundland and Labrador Legacy Nature Trust was not incorporated until 14 September 1999, 5 months after the cheque was issued on an urgent basis.
- the \$1 million cheque remained in the possession of government officials from 31 March 1999 until it was deposited on 13 May 1999, 61 days after the \$1 million was urgently required and still before the entity was created.
- Government deposited the cheque on 13 May 1999 to a bank account called the "Consolidated Tender Account" which is under the direct control of the Treasury Board Secretariat. This bank account holds bid deposits required by Government from bidders as a condition of tender calls, a purpose completely unrelated to this \$1 million cheque.

### 3.24 Legacy Nature Trust

#### Conclusion

It concerns me that Government has circumvented the *Financial Administration Act* by issuing a cheque for \$1 million on an urgent basis on the last day of the fiscal year to a corporation which did not exist. I am also concerned that this cheque was in the possession of Government officials for 43 days before it was deposited. When it was finally deposited, it was held in a bank account used for bid deposits which accompany public tenders, a purpose entirely unrelated to the nature of the cheque.

#### Department's Response

*I would like to make the following comments:*

- *I cannot agree that Government circumvented the Financial Administration Act by issuing a cheque for \$1 million on an urgent basis to the Newfoundland and Labrador Legacy Nature Trust (the Trust). It was always understood that the Trust would be formally established in very short order.*
- *To create the Trust involved the creation of a corporate entity and legal documents including legal costs which the founding members of the Trust were not prepared to undertake without the commitment of Government that the funding was in place.*
- *It only became apparent early in the fiscal year that the creation of the necessary trust and incorporation documents acceptable to both Government and the proposed Trust members would take longer than anticipated. During the period of this determination, the cheque was locked away for safe keeping in the executive offices.*
- *Often in such cases, cheques are forwarded to legal counsel to be held in trust with interest accruing to the payee. In this case, to ensure a level of further urgency to the Trust and to provide better accountability and cost management of the funds, in discussions with the Comptroller General's office, it was agreed that it was in Government's best interest to identify an appropriate Government Trust Account to hold the funds until such time as the necessary agreements were in place between Government and the Trust.*

### 3.24 Legacy Nature Trust

- *As I understand it, the "Consolidated Tender Account" is a Trust Account in the province's name which would allow for a speedy transfer of funds to the Trust upon final agreement by Government and the Trust of the accountability conditions to be included in the Trust and the final Trust documents. Notwithstanding what the Government Trust Account was normally used for, it was and still remains to be a valuable tool to ensure appropriate accountability and control over Government funds.*
- *Given the situation as outlined previously, I wish to advise that the funds have been re-deposited in the Consolidated Revenue Fund and final payment will not be made until the formal Trust is in place with the required accountability framework finalized. This is expected in the very near future.*

*In summary, this department views its handling of the Trust funds as more than acceptable and prudent. Obviously with any contribution of this nature and amount, there have to be developed criteria and conditions to ensure an appropriate accountability by the Trust. The development of the specific conditions which eventually required Cabinet review and ratification took longer than anticipated.*

#### **Treasury Board Secretariat's Response**

*It is my view that the requirements of the Financial Administration Act (FAA) were complied with and I refer you to my comments on your report paragraph dealing with the issue of Special Warrants. I note that the Department of Forest Resources and Agrifoods will be responding on the details related to the Legacy Nature Trust.*

*This Special Warrant had been issued with the intention to provide funding to establish the Legacy Nature Trust. The trust would have access to external sources of funds not accessible by Government. Unfortunately, the finalization of that trust was delayed as noted. Given this delay, as well as the information resulting from your review of this matter, we do not feel that this expenditure should now represent a charge against the 1998-99 year. Steps have been taken to have the money deposited back into the Consolidated Revenue Fund. Once arrangements are finalized, payment will be made in the current fiscal year.*



### 3.25 Newfoundland Farm Products Corporation

#### Introduction

Newfoundland Farm Products Corporation was established in 1963 under the *Farm Products Corporation Act*. As a Provincial Crown corporation, Newfoundland Farm Products Corporation produced a full range of chicken products which were marketed throughout the Province, the Maritimes and central Canada. The Corporation operated two federally inspected abattoir complexes in the Province, one in St. John's and one in Corner Brook. In 1996-97, the last full year of operation, the Corporation processed 8.0 million chickens resulting in 11.8 million kilograms of saleable product. The Corporation employed approximately 275 people and had an annual payroll of \$10.2 million. Over a ten year period from 1987-88 to 1996-97, the Corporation incurred average annual operating losses of \$4.3 million.

A new Board of Directors was appointed in November 1996 and given the mandate to pursue privatization of the Corporation. On 17 June 1997, Newfoundland Farm Products entered into an Agreement of Purchase and Sale with IPL Processing Limited, a subsidiary of Integrated Poultry Limited, and a Share Purchase Agreement with Integrated Poultry Limited and IPL Processing Limited. These agreements provided for the sale of the St. John's processing facility to IPL Processing Limited effective 4 October 1997. In October 1997, the sale of the St. John's processing operation to Integrated Poultry Limited, a consortium of local chicken producers, was concluded. The processing operations in Corner Brook were closed by Government in April 1997.

#### Scope and Objectives

We conducted a review of the Newfoundland Farm Products Corporation during 1997. During 1998, we conducted a follow-up review. Since the terms and conditions of the purchase and sale agreement are still being realized, and the divestiture process of Newfoundland Farm Products Corporation is continuing, it was decided to conduct another follow-up review of the Corporation. The objectives of our review were to:

- review compliance with the terms and conditions of the purchase and sale agreement between Newfoundland Farm Products Corporation and Integrated Poultry Limited; and
- review transactions between Government, Newfoundland Farm Products Corporation, and Integrated Poultry Limited during the period April 1998 to September 1999.

We completed our review of the Corporation in November 1999.

### **3.25 Newfoundland Farm Products Corporation**

#### **Conclusions**

On 17 June 1997, Newfoundland Farm Products Corporation entered into an Agreement of Purchase and Sale with IPL Processing Limited and a Share Purchase Agreement with Integrated Poultry Limited and IPL Processing Limited. These agreements provided for the sale of the St. John's chicken processing facility to IPL Processing Limited effective 4 October 1997.

Financial and other assistance has been provided by Government to Integrated Poultry Limited since 1997 as follows:

- In 1997, Government provided \$8.5 million in operating and capital grants to Integrated Poultry Limited.
- Under the terms of the Purchase and Sale Agreement and the subsequent Share Purchase Agreement, Integrated Poultry Limited was to pay \$2.0 million to Newfoundland Farm Products Corporation for \$1.4 million for inventory and \$0.6 million for operating losses incurred when Newfoundland Farm Products Corporation was jointly managed by Government and IPL.

On 4 October 1997, \$500,000 of the \$0.6 million due to Government for operating losses incurred when Newfoundland Farm Products Corporation was jointly managed by Government and IPL was repaid. As at March 1999, the remaining \$1.5 million was still owing to Government. In January 1999, Government and Newfoundland Farm Products Corporation agreed to restructure the repayment terms on the \$1.5 million note receivable from Integrated Poultry Limited. Repayments were originally due to commence in January 1999 but have been restructured to be repaid over a 12 month period, commencing in January 2000.

- In October 1997, Government provided a \$10.0 million term loan guarantee to Integrated Poultry Limited. In December 1998, Government increased the \$10.0 million loan guarantee by \$1.5 million for a total of \$11.5 million.
- In October 1997 Government provided a working capital deficiency loan guarantee for \$1.0 million.
- In December 1998, Government also issued a new loan guarantee in the amount of \$400,000 which has since been repaid.
- In April 1999, Integrated Poultry Limited requested Newfoundland Farm Products Corporation to provide the initial financing up to \$1.7 million to purchase a grain shipment. Newfoundland Farm Products Corporation paid for this shipment

### 3.25 Newfoundland Farm Products Corporation

by borrowing \$1.5 million from a bank as authorized by the Lieutenant-Governor in Council. This loan was guaranteed by the Province. In May 1999, Integrated Poultry Limited repaid the \$1.5 million to Newfoundland Farm Products Corporation and the related loan guarantee by the Province was canceled.

- In October 1999, IPL requested Newfoundland Farm Products Corporation to provide financing for another shipment of grain. In November 1999, the Lieutenant-Governor in Council authorized Newfoundland Farm Products Corporation to borrow up to \$1.7 million to purchase the grain shipment. This loan was guaranteed by the Province. The loan is to be repaid by 31 May 2000 from the proceeds of the sale of the grain to IPL Processing Limited and/or other customers as deemed appropriate. At the end of our review, Newfoundland Farm Products Corporation had borrowed \$1.4 million towards this grain shipment.
- In October of each year, Integrated Poultry Limited is to remit an annual loan guarantee fee, in the amount of 1% of the outstanding loan guarantee, to the Department of Finance. In March 1999, Integrated Poultry Limited did not have sufficient cash to pay the loan guarantee fees of \$110,000 which was owing from 1998 and the 1999 loan guarantee fee of \$126,000 which was to be billed in October 1999. At IPL's request, Government agreed to receive monthly payments of \$20,000 commencing 1 April 1999 until both amounts due are paid in full. Our review disclosed that monthly payments of \$20,000 were received from April 1999 to September 1999 and totalled \$120,000.

In preparing its 31 March 1999 financial statements, Government determined, in December 1999, that it will most likely have to honour its \$12.8 million loan guarantee for Integrated Poultry Limited. As a result, included in the Province's liabilities in the Consolidated Revenue Fund Financial Statements for the year ended 31 March 1999 is a provision of \$12.8 million for possible losses on the \$12.8 million loan guarantee.

During 1998-99, in order for IPL to obtain financing, Government relinquished a portion of its security on the assets of Integrated Poultry Limited.

In April 1999, Government requested a national poultry producer to perform a review of the viability of Integrated Poultry Limited and the Newfoundland poultry industry as a whole. Also in April 1999, the Board of Newfoundland Farm Products Corporation engaged Ernst & Young Inc. to prepare a high level report, outlining various scenarios, and the actions to be taken by Government in the event of bankruptcy of IPL.

### **3.25 Newfoundland Farm Products Corporation**

On 6 October 1999, the Minister of Finance was informed that the Bank of Nova Scotia had issued a Notice of Default to IPL Processing Limited for credit facilities provided to IPL by way of a commitment letter dated 21 December 1998. The bank, at the specific request of the Province as Guarantor, consented and entered into an agreement to "standstill" on its right to issue a demand for payment of its loans until 4 December 1999 to provide additional time for IPL to negotiate with potential investors and/or restructure its debt.

On 15 December 1999, the bank demanded payment, by 7 January 2000, from Integrated Poultry Limited for its loans and issued a "Notice of Intention to Enforce Security". As a result, on 16 December 1999, Government paid the \$11.5 million under guarantee to the bank and for the \$1.0 million guarantee, elected to require the bank to realize upon its security and to notify the Government of the amount of any deficiency up to the \$1.0 million guarantee. On 20 December 1999, Government demanded payment of the \$11.5 million from Integrated Poultry Limited and on 21 December 1999, Government issued a "Notice of Intention to Enforce Security" to Integrated Poultry Limited.

In late December 1999, Government and the bank formed a secured Creditor Committee and on 10 January 2000, Government, the bank and Integrated Poultry Limited signed a Forbearance Agreement which will expire on 31 January 2000 unless it is extended. The purpose of this Agreement is to allow Integrated Poultry Limited the opportunity to continue its search for new equity or other investors, without being subject to further action by Government and the bank with respect to exercising their security in the interim, as well as to operate in the manner permitted by the Agreement. Under this Agreement, if Integrated Poultry Limited is unsuccessful in restructuring its debt or attracting a new investor, Integrated Poultry Limited has agreed that it will not oppose Government and the bank should they choose to realize upon their security by requesting the Courts to appoint a Receiver.

#### **Detailed Findings      Financial Assistance Provided by Government**

The following summarizes the financial assistance provided by Government to Integrated Poultry Limited since the company assumed operation of the chicken production facilities in October 1997.

##### **1. \$8.5 Million in Grants**

In 1997, when Integrated Poultry Limited assumed operation of the chicken production facilities, Government provided grants totalling \$8.5 million. Of this amount, \$4.5 million was for operations while the remaining \$4.0 million was for capital infrastructure.

### **3.25 Newfoundland Farm Products Corporation**

#### **2. \$1.5 Million Owed to Newfoundland Farm Products Corporation by IPL**

Under the terms of the Purchase and Sale Agreement and the subsequent Share Purchase Agreement, Integrated Poultry Limited was to pay \$2.0 million to Newfoundland Farm Products Corporation for the following:

- \$983,819 for saleable product inventory, repayable in three equal monthly instalments commencing January 1999;
- \$393,993 for packaging and raw materials inventory, repayable in three equal monthly instalments commencing March 1999; and
- \$658,773 for operating losses incurred when Newfoundland Farm Products Corporation was jointly managed by Government and IPL, repayable in one instalment of \$500,000 due in October 1997 with the remaining balance of \$158,773 repayable in five equal monthly instalments commencing May 1999.

On 4 October 1997, the \$500,000 due to Government for operating losses incurred when Newfoundland Farm Products Corporation was jointly managed by Government and IPL, was repaid. As at March 1999, the remaining \$1.5 million was still owing to Government. In January 1999, Government and Newfoundland Farm Products Corporation agreed to restructure the repayment terms on the \$1.5 million note receivable from Integrated Poultry Limited. Repayments were originally due to commence in January 1999 but have been restructured to be repaid over a 12 month period, commencing in January 2000.

#### **3. \$11.5 Million Term Loan Guarantee to Integrated Poultry Limited**

The June 1997 Share Purchase Agreement specified various terms and conditions related to the \$10.0 million term loan guarantee provided by Government in October 1997 to Integrated Poultry Limited. Specifically, Integrated Poultry Limited was required to provide the following to the Minister of Finance:

- Annual audited financial statements for Integrated Poultry Limited, IPL Processing Limited, and IPL Production Limited are required within 90 days of year end. Government has not received any annual audited financial statements for these entities.



### 3.25 Newfoundland Farm Products Corporation

- Annual consolidated financial statements are also required from Integrated Poultry Limited within 90 days of the June year end (i.e. end of September). However, the only audited consolidated financial statements received by Government was from IPL Processing Limited for the 1997-98 year which were received on 26 March 1999. The 1998-99 audited consolidated financial statements should have been received from Integrated Poultry Limited by 24 September 1999; however, they have not been received as of 15 November 1999.
- IPL is required to provide the following information on a monthly basis within 30 days of month end:
  - unconsolidated and consolidated financial statements;
  - information on the status of the outstanding loan guaranteed by the Province particularly as it relates to payments on such loans;
  - summary information on capital expenditures; and
  - detailed summary of contract activity by major capital expenditure component, particularly as it relates to cost versus budget.

With the exception of monthly unconsolidated financial statements, all of the above information is being received by Newfoundland Farm Products Corporation and is being discussed with IPL during regular meetings.

In December 1998, Government increased the \$10.0 million term loan guarantee issued in October 1997 by \$1.5 million for a total of \$11.5 million.

In September 1998, the Board of Directors of Newfoundland Farm Products Corporation suggested that a representative of the Department of Finance be asked to sit on the Board of Newfoundland Farm Products Corporation as an observer. An Assistant Deputy Minister of the Department of Finance was subsequently appointed a Member and Secretary of the Board of Newfoundland Farm Products Corporation.

During 1999, the Board of Directors of Newfoundland Farm Products Corporation have met with officials of IPL on a monthly basis to review the operations of IPL. Documentation provided by IPL was on file at the Department of Finance.



### **3.25 Newfoundland Farm Products Corporation**

#### **4. \$1.0 Million Working Capital Deficiency Loan Guarantee to Integrated Poultry Limited**

In October 1997, and subsequent to the Purchase and Sale Agreement, Government provided a working capital deficiency loan guarantee for \$1.0 million.

#### **5. \$400,000 Loan Guarantee to Integrated Poultry Limited**

In December 1998, Government issued a new loan guarantee in the amount of \$400,000. This amount has since been repaid.

#### **6. Financing of Grain Shipments**

In April 1999, Integrated Poultry Limited requested Newfoundland Farm Products Corporation to provide the initial financing up to \$1.7 million to purchase a grain shipment. Newfoundland Farm Products Corporation paid for this shipment by borrowing \$1.5 million from a bank as authorized by the Lieutenant-Governor in Council. This loan was guaranteed by the Province.

In order for Integrated Poultry Limited to purchase the \$1.5 million grain shipment from Newfoundland Farm Products Corporation, Integrated Poultry Limited entered into an equity investment, with redeemable terms, with a private corporation. To facilitate the agreement between Integrated Poultry Limited and this private corporation, in May 1999, Cabinet authorized the Minister of Finance to execute a confirmation agreement to release the Province's second security position on the assets of IPL Production Limited, (a subsidiary of IPL Processing Limited) located at Long Pond, Manuels under the following terms and conditions:

- the release of security on the same assets by a lending institution;
- the release of security will only be undertaken if the assets are transferred to the private corporation, with whom Integrated Poultry Limited had arranged a \$1.7 million equity investment, with redeemable terms, for the purpose of providing public grain storage in Eastern Newfoundland; and
- the \$1.7 million proceeds from the equity investment between Integrated Poultry Limited and the private corporation are used to pay all costs for the grain shipment purchased by Newfoundland Farm Products Corporation which was stored with IPL Production Limited, pursuant to a Grain Agreement, dated 7 May 1999 between IPL Production Limited and Newfoundland Farm Products Corporation.

### **3.25 Newfoundland Farm Products Corporation**

In May 1999, Integrated Poultry Limited repaid the \$1.5 million to Newfoundland Farm Products Corporation and the related loan guarantee by the Province was canceled.

In October 1999, IPL requested Newfoundland Farm Products Corporation to provide financing for another shipment of grain. In November 1999, the Lieutenant-Governor in Council authorized Newfoundland Farm Products Corporation to borrow up to \$1.7 million to purchase the grain shipment. This loan was guaranteed by the Province. The loan is to be repaid by 31 May 2000 from the proceeds of the sale of the grain to IPL Processing Limited and/or other customers as deemed appropriate. At the end of our review, Newfoundland Farm Products Corporation had borrowed \$1.4 million towards this grain shipment.

#### **7. \$3.5 Million Financial Package for Integrated Poultry Limited**

In December 1998, Government agreed to participate in a \$3.5 million financial package for Integrated Poultry Limited. Government's involvement in this financial package included the following:

- an increase of \$1.5 million in Government's \$10.0 million term loan guarantee which was issued in October 1997 and which was previously discussed in item #3;
- \$400,000 loan to IPL, guaranteed by Government, repayable directly from a reduction in shareholder quota lease payments over a 12 month period after the date of issue as previously discussed in item #5;
- \$200,000 of shareholder contributions to be released from the Quota Holders Trust Fund, which is under the trusteeship of the Minister of Finance;
- \$1.0 million loan to IPL from a lending institution subject to Government subordinating its security over IPL feed mill and grain storage in favour of the lending institution in order to arrange financing, and with Government to subordinate its \$1.0 million in personal guarantees from IPL shareholders, in favour of \$500,000 in personal guarantees to be provided by IPL shareholders to the lending institution. This is discussed under the section in this report on Government Security on Loan Guarantees.

### **3.25 Newfoundland Farm Products Corporation**

As part of the financial package, Government included a number of conditions on its participation as follows:

- IPL is to actively solicit prospective equity investors and an experienced Chief Operating Officer, with Government representatives to take a lead role in this process;
- The \$1.5 million owed to Newfoundland Farm Products Corporation by IPL, on which payment was to commence in January 1999, and which was discussed in item #2 be restructured to be payable within 24 months with payments to commence not later than January 2000;
- Contributions to the Quota Holders Trust Fund will be deferred for a 12 month period to accommodate repayment of the \$400,000 loan; and
- IPL will meet with Government on an as required basis to provide any and all information which Government may request to assist with monitoring of IPL operations.

#### **8. Loan Guarantee Fees**

In October of each year, Integrated Poultry Limited is to remit an annual loan guarantee fee, in the amount of 1% of the outstanding loan guarantee, to the Department of Finance. The first payment of \$110,000 (1% of \$11.0 million in total loan guarantees) was to be made in October 1998. With the increase in the loan guarantees of \$1.5 million and \$400,000 in January 1999, the 1999 loan guarantee fee, which was to be billed in October 1999, increased to \$126,000.

In a letter to the Department of Finance dated 18 March 1999, Integrated Poultry Limited indicated that they did not have sufficient cash to pay the loan guarantee fees of \$110,000 which was owing from 1998 and the 1999 loan guarantee fee of \$126,000. At IPL's request, Government agreed to receive monthly payments of \$20,000 commencing 1 April 1999 until both amounts due are paid in full. Our review disclosed that monthly payments of \$20,000 were received from April 1999 to September 1999 and totalled \$120,000.

### **3.25 Newfoundland Farm Products Corporation**

#### **Government Security on Loan Guarantees**

As security for the loan guarantees that the Province provided to IPL, it took a first charge on certain assets of the Corporation. These included:

- first charge on the assets at the Pleasantville site;
- first charge on the assets at Cochrane Pond;
- first charge on real and personal property of the feed mill production facility in Mount Pearl and the grain storage facility in Conception Bay South;
- first charge on production licences/quotas;
- subordinate charge on all assets secured by the bank (receivables and inventory);
- second charge on all other assets of IPL; and
- \$1.0 million personal guarantees from the IPL shareholders.

However, in August 1998, in order for IPL to obtain financing with a lending institution, Government relinquished a portion (\$2.1 million) of its security on the real and personal property of the feed mill production facility in Mount Pearl and the grain storage facility in Conception Bay South.

Subsequently, in January 1999, in order for IPL to obtain an additional \$1.0 million financing, Government subordinated its remaining security over the real and personal property of the feed mill production facility in Mount Pearl and the grain storage facility in Conception Bay South in favour of the lending institution. Government also subordinated \$500,000 of its \$1.0 million in personal guarantees from IPL shareholders, in favour of the lending institution.

In preparing its 31 March 1999 financial statements, Government determined, in December 1999, that it will most likely have to honour its \$12.8 million loan guarantee for Integrated Poultry Limited. As a result, included in the Province's liabilities in the Consolidated Revenue Fund Financial Statements for the year ended 31 March 1999 is a provision of \$12.8 million for possible losses on the \$12.8 million loan guarantee.

### 3.25 Newfoundland Farm Products Corporation

#### **Review of the Viability of Integrated Poultry Limited and the Newfoundland Poultry Industry**

In April 1999, Government requested a national poultry producer to perform a review of the viability of Integrated Poultry Limited and the Newfoundland poultry industry as a whole. Government officials indicated that this producer agreed, at its own expense, to do a cursory review of the viability of Integrated Poultry Limited and the producer selected KPMG to assist them with this initiative. The two prime objectives of the review were:

- to understand the cost structure of producing poultry within Newfoundland and benchmark this against other Canadian provinces and American production costs; and
- based on farm gate prices and price to the distributor, determine the maximum acceptable processing costs and evaluate Integrated Poultry Limited with a view to achieving this cost.

The review was to begin in April 1999 and be completed by the end of May 1999. Government officials indicated that the producer was not prepared to release any written documentation of its findings to Government.

Also in April 1999, the Board of Newfoundland Farm Products Corporation engaged Ernst & Young Inc. to prepare a high level report, outlining various scenarios, and the actions to be taken by Government in the event of bankruptcy of IPL. Ernst & Young Inc. performed a number of initiatives to provide the Board with a high level review of Government relative security positions, areas of primary concern, and possible actions to be taken should IPL become insolvent. The cost associated with this engagement was anticipated in the range of \$35,000 to \$50,000. A report from Ernst & Young Inc. was issued on 14 June 1999. Based on the report, the Board indicated that it would provide further instruction and identify areas where it would require further analysis.

In May 1999, the Board of Newfoundland Farm Products Corporation supported the process outlined by KPMG, the auditors of IPL, to attract a new investor for IPL. It was indicated that the process should be completed in three months at a cost to IPL of \$50,000 to \$100,000. The Board supported the process provided the engagement of KPMG did not delay or cancel the evaluation performed by the national poultry producer.

### **3.25 Newfoundland Farm Products Corporation**

#### **IPL Processing Limited Default**

On 6 October 1999, the Minister of Finance was informed that the Bank of Nova Scotia had issued a Notice of Default to IPL Processing Limited for credit facilities provided to IPL by way of a commitment letter dated 21 December 1998. Although the commitment letter did not require the bank to provide IPL with notice of any default, since the advances are payable on demand, the bank formally advised IPL of its concerns and to put IPL on notice that the bank was not prepared to continue making credit facilities available unless the defaults were rectified by 27 October 1999. The letter of default was acknowledged by the Minister of Finance.

These defaults were not rectified by 27 October 1999 and, although the bank had a legal right to demand payment, the bank, at the specific request of the Province as Guarantor, consented and entered into an agreement to "standstill" on its right to issue a demand for payment of its loans until 4 December 1999 to provide additional time for IPL to negotiate with potential investors and/or restructure its debt.

On 15 December 1999, the bank demanded payment, by 7 January 2000, from Integrated Poultry Limited for its loans and issued a "Notice of Intention to Enforce Security". As a result, on 16 December 1999, Government paid the \$11.5 million under guarantee to the bank and for the \$1.0 million guarantee, elected to require the bank to realize upon its security and to notify the Government of the amount of any deficiency up to the \$1.0 million guarantee. On 20 December 1999, Government demanded payment of the \$11.5 million from Integrated Poultry Limited and on 21 December 1999, Government issued a "Notice of Intention to Enforce Security" to Integrated Poultry Limited.

In late December 1999, Government and the bank formed a secured Creditor Committee and on 10 January 2000, Government, the bank and Integrated Poultry Limited signed a Forbearance Agreement which will expire on 31 January 2000 unless it is extended. The purpose of this Agreement is to allow Integrated Poultry Limited the opportunity to continue its search for new equity or other investors, without being subject to further action by Government and the bank with respect to exercising their security in the interim, as well as to operate in the manner permitted by the Agreement. Under this Agreement, if Integrated Poultry Limited is unsuccessful in restructuring its debt or attracting a new investor, Integrated Poultry Limited has agreed that it will not oppose Government and the bank should they choose to realize upon their security by requesting the Courts to appoint a Receiver.



### 3.25 Newfoundland Farm Products Corporation

#### Other Issues

##### 1. Debt of Newfoundland Farm Products Corporation Assumed by Government

At the time of our 1998 review, Newfoundland Farm Products Corporation had a demand loan of \$10.2 million guaranteed by the Province. In January 1999, Government assumed the \$10.2 million debt of Newfoundland Farm Products Corporation and it is now recorded as a direct debt of the Province. Interest for the period 1 April 1998 to 25 February 1999 totalling \$624,000 was reimbursed to Newfoundland Farm Products Corporation.

##### 2. Board Meetings

The Board of Directors of Newfoundland Farm Products Corporation are appointed by Lieutenant-Governor in Council. In accordance with the *Farm Products Corporation Act*, the Board is to be comprised of not fewer than 5 members and no more than 9 members. Effective 1 January 1999, the Board consisted of 6 members. During the period January 1999 and 15 November 1999 the Board held 24 meetings. Minutes are kept for all Board meetings.

During our review of the minutes of the Board meetings, we found reference to a letter of resignation from one Board member dated 27 May 1999. In the letter of resignation, the Board member felt that it was an opportune time to resign because he was not heavily involved in the matters of the Corporation and indicated that, to his knowledge, the Board had not met during 1999. However, from January 1999 to the date of the letter of resignation on 27 May 1999, the Board held 14 meetings. A review of the Board minutes indicated that this member was not present at any of these 14 meetings.

A review of the Board minutes of the 24 meetings held between January 1999 and November 1999 indicated that another Board member attended only 2 meetings.

#### Department's Response

*The report provided by the Auditor General accurately reflects Government's and Newfoundland Farm Products Corporation involvement with Integrated Poultry Limited. Most importantly it certainly highlights the efforts of Government to provide for a continued poultry industry in this Province and the level of detailed monitoring and accountability of Integrated Poultry Limited by senior officials and government agencies.*

### 3.25 Newfoundland Farm Products Corporation

*As for your observation that Government has not received audited unconsolidated financial statements of Integrated Poultry Limited, IPL Processing Limited and IPL Production Limited, I must advise that Integrated Poultry Limited only prepares annual consolidated financial statements, which are the most relevant to its accounting practices and loan agreements. Furthermore, it is also the most appropriate from a monitoring perspective. In hindsight, an amendment to the original Share Purchase Agreement should have been made to delete the requirement for annual audited financial statements of the unconsolidated companies. It should also be noted that the audit work for the June 1999 financial statements has been concluded by the company's auditor for quite some time, however, the auditors were not prepared to release their final audit report pending the outcome of the company's investment search.*

### 3.26 Management of Crown Land

#### Introduction

The Department of Government Services and Lands is responsible for the management of the Province's Crown lands. Crown lands comprise approximately 95% of the Province's land mass and as such is one of the Province's most significant natural resources. The management of Crown land is assigned to the Lands Branch of the Department of Government Services and Lands. This Branch is comprised of three Divisions: Crown Lands Administration, Surveys and Mapping, and Land Management. The Branch's responsibilities include processing land applications, preventing unauthorized use of Crown land, resolving conflicts in land use and ownership, producing a map inventory of land in the Province, and developing land use policy and management plans. Figure 1 outlines the expenditures of these Divisions and the related revenue for the five years ended 31 March 1999.

Figure 1

#### Expenditure and Revenue Lands Branch 31 March (\$000's)

|                                  | 1995           | 1996           | 1997             | 1998             | 1999           |
|----------------------------------|----------------|----------------|------------------|------------------|----------------|
| <b>Expenditure</b>               |                |                |                  |                  |                |
| Crown Lands Administration       | \$2,437        | \$2,346        | \$2,896          | \$2,344          | \$2,439        |
| Surveys and Mapping              | 908            | 927            | 870              | 903              | 847            |
| Land Management                  | 280            | 479            | 420              | \$567            | 825            |
| <b>Total expenditure</b>         | <b>\$3,625</b> | <b>\$3,752</b> | <b>\$4,186</b>   | <b>\$3,814</b>   | <b>\$4,111</b> |
| <b>Revenue</b>                   |                |                |                  |                  |                |
| Crown Land Fees and Sales        | \$546          | \$400          | \$4,827          | \$5,371          | \$1,867        |
| Land Lease Rentals               | 1,662          | 1,675          | 1,481            | 2,121            | 1,896          |
| Other                            | 661            | 387            | 1,049            | 1,178            | 614            |
| <b>Total revenue</b>             | <b>\$2,869</b> | <b>\$2,462</b> | <b>\$7,357</b>   | <b>\$8,670</b>   | <b>\$4,377</b> |
| <b>Net expenditure (revenue)</b> | <b>\$756</b>   | <b>\$1,290</b> | <b>(\$3,171)</b> | <b>(\$4,856)</b> | <b>(\$266)</b> |

Source: Consolidated Revenue Fund Financial Statements

To assist in the management of Crown lands, there are four Regional Offices located in St. John's, Gander, Corner Brook and Goose Bay.



### 3.26 Management of Crown Land

#### Introduction

The Department of Government Services and Lands is responsible for the management of the Province's Crown lands. Crown lands comprise approximately 95% of the Province's land mass and as such is one of the Province's most significant natural resources. The management of Crown land is assigned to the Lands Branch of the Department of Government Services and Lands. This Branch is comprised of three Divisions: Crown Lands Administration, Surveys and Mapping, and Land Management. The Branch's responsibilities include processing land applications, preventing unauthorized use of Crown land, resolving conflicts in land use and ownership, producing a map inventory of land in the Province, and developing land use policy and management plans. Figure 1 outlines the expenditures of these Divisions and the related revenue for the five years ended 31 March 1999.

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| <b>Revenue</b>                   |                |                |                  |                  |                |
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| <b>Net expenditure (revenue)</b> | <b>\$756</b>   | <b>\$1,290</b> | <b>(\$3,171)</b> | <b>(\$4,856)</b> | <b>(\$266)</b> |

Source: Consolidated Revenue Fund Financial Statements

To assist in the management of Crown lands, there are four Regional Offices located in St. John's, Gander, Corner Brook and Goose Bay.

### **3.26 Management of Crown Land**

#### **Scope and Objectives**

We completed our review of the management of Crown lands in September of 1999. The objectives of our review were to determine whether there are adequate systems and procedures to:

- identify Crown land and determine how the land is being utilized;
- develop and coordinate provincial land use management plans;
- dispose of Crown land in accordance with legislation and Departmental policies; and
- identify Crown land leases, licences and grants, to ensure these lands are being utilized as intended and to maintain appropriate billing and collection procedures over this area.

#### **Conclusions**

The Department of Government Services and Lands is responsible for the management of the Province's Crown lands. Crown lands comprise approximately 95% of the Province's land mass and as such is one of the Province's most significant natural resources. Our review of the Department's management of Crown lands indicated the following:

- There is no comprehensive and complete land parcel identification system for all land in the Province and therefore, Government does not know the extent or boundaries of Crown lands in the Province. As a result, it is more difficult for Government to effectively manage and plan the use of Crown lands, and Government's land allocation and designation processes are more extensive and time consuming.
- The Province does not have comprehensive land use policies to facilitate a co-ordinated approach for land use within Government. As a result, planning for land use within Government is fragmented and covers only small areas of the Province. Discussions with Departmental officials indicated that a comprehensive land plan for the entire Province is not practical due to the significant costs involved. However, it would be prudent for Government to complete comprehensive land plans for certain areas of the Province including those areas where potential for conflict over land use exists.
- The following observations were noted with respect to application processing:
  - A review of 22 selected land applications indicated that, in general, applications are being processed in accordance with legislation and Departmental policy.



### 3.26 Management of Crown Land

- A recent Departmental report on the Crowns Land Division recognized a number of areas that cause delays in the application process that could be improved including the process for referring applications to other Government departments and agencies and the process of referring applications from the Government Service Centres to the Regional Lands Offices.
- Information maintained in the Department's system that tracks the progress of an application is often inaccurate. This reduces the usefulness of the information to monitor the status of applications. Discussions with staff in the Regional Offices also indicated that they do not generally review the reports available from the system to monitor applications nor do they generally monitor the status of applications.
- A sample of 30 dispositions of Crown land indicated that for the sample selected, adequate information, in the form of appraisals performed either by the Municipal Assessment Agency or by Departmental staff, was available to support the fair market value assessed on the property.
- The Land Management Division does not maintain adequate information on cottage lot developments, including the status of the lot sales and the associated costs and revenues. Accurate and complete information on status of the development and associated costs and revenues would enhance information available to Management for the monitoring of existing developments and the planning of future developments.
- Companies that have approved status under the *Economic Diversification and Growth Enterprises Act* have been approved to lease certain Crown land at \$1. Although Departmental officials were aware that a number of EDGE companies had leased Crown land at \$1, they could not provide us with any information regarding which EDGE companies had leased this land, what land had been leased, or what the land was being used for. The Department of Industry, Trade and Technology, who are responsible for administering the EDGE program, also could not provide us with any of this information. Thus, there has been no monitoring of the status of this land or whether these companies still have eligible EDGE status. We also noted that there is nothing in the agreements between Government and EDGE companies to address what would happen to this land if the company lost its EDGE status.

### 3.26 Management of Crown Land

After significant effort by staff of the Department a list of EDGE companies that are leasing Crown land at \$1 was provided to us. A comparison of this list with those EDGE companies that have had their status revoked indicated that all of the companies that are leasing Crown land for \$1 still have EDGE status.

- Monitoring procedures to ensure that the lessee has adhered to the terms of the lease with respect to type of development and period to complete development, is usually limited to sending out affidavits to individuals, after five years have lapsed, which the individual completes to attest to the fact they have adhered to these terms. We also noted that some of the Regional Offices are not even sending out these affidavits. As a result, the Department cannot determine whether Crown land is being used for the purposes intended when the land was authorized for disposition.
- Although a review of a sample of leases indicated that billings were properly prepared and recorded in the accounting records, we noted that for those leases where title to the land will only be transferred to the lessee after the lease is paid off over 5 years, the Department has only recorded the current portion or 1/5 of the balance owing in the accounting records.

We noted weaknesses with respect to the collection of accounts. More specifically \$1.3 million or 48% of the accounts receivable at 31 March 1999 of \$2.7 million were in excess of one year overdue. The Department does not monitor these accounts nor does it perform any regular collection activity.

- The Province has been developing an implementation plan for the establishment of geographic information systems (GIS) throughout Government. These computer systems will allow users to collect, manage and analyze large volumes of data related to geographically referenced data and information. The Department has converted information from the manual Crown Titles System into a digital format for use in a GIS system. However, the Department has been completing the development of this system without an approved Provincial Geomatics Strategy in place. In addition, we noted that the system that was converted contained incomplete Crown Titles information and outdated information with respect to base mapping. As a result, the new digitized information is also incomplete and outdated.

### 3.26 Management of Crown Land

#### Findings and Recommendations

#### Identification and Use of Crown Lands

In order to effectively manage and plan for the use of Crown lands, the Department must have adequate information systems to identify Crown land and how it is currently being used. Since the early 1970s there have been a number of reviews, both internal and external to the Department, that have identified the inability of Government's land information systems to provide this information. The reviews that came to our attention during our audit are outlined in Figure 2.

One of the main reasons that this information is not available is that, in contrast to most other Provinces, land registration is not compulsory in this Province. In addition, many land titles have their basis in unregistered adverse possession against the Crown. As a result, Government cannot identify all private land holdings and thus, cannot identify the extent or boundaries of Crown land.

In addition, some Crown land ownership is disbursed among a variety of departments and although some land ownership information is available, it resides in a wide variety of systems maintained by different departments. The Department has indicated that although there is a database in the Department of Works, Services and Transportation that lists lands transferred from the Department of Government Services and Lands (public lands), not all lands transferred particularly prior to 1980, are recorded in this database. As a result, the Department is unable to account for a complete inventory of all Crown land that has been transferred to other departments and agencies.

Figure 2

#### Reviews on Crown Lands

| Date of Review | Name of Review                                                                     | Objective of Review                                                                                                                                                                                                                                                                      |
|----------------|------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1973           | Task Force Report                                                                  | To review land use in the Province.                                                                                                                                                                                                                                                      |
| 1978           | Study by Decision Dynamics Corporation                                             | Study of land ownership information.                                                                                                                                                                                                                                                     |
| 1994           | Report of the Interdepartmental Review Committee on "Land Use" Policy and Planning | 1) To establish an approach for the development of a comprehensive land use policy framework for the Province; 2) to identify a specific administrative mechanism to achieve enhanced co-ordination and integration of land use planning activity and decision-making within government. |
| 1996           | Program Review                                                                     | To review all programs of the Departments.                                                                                                                                                                                                                                               |

Source: Department of Government Services and Lands

### 3.26 Management of Crown Land

In 1975 the Lands Branch developed a central repository of land use information in the form of a Land Use Atlas. This improved the availability of information on land use; however, this information is still not complete or maintained on a timely basis. For example, the Atlas references lands that were temporarily designated for certain purposes but many of these temporary designations no longer exist and the Atlas has not been updated to reflect these changes.

Although the Department has a digitized land parcel identification system for land where Crown title has been issued, this system is not complete as Government does not know the extent or boundaries of Crown lands nor does it contain complete information on lands that have been transferred to other Government departments and agencies. Without complete and comprehensive information on land ownership and use, it is more difficult for Government to effectively manage and plan the use of Crown land and Government's land allocation and designation processes are more extensive and time consuming.

#### Land Use Policy and Planning

Land in the Province is classified into one of five categories as follows:

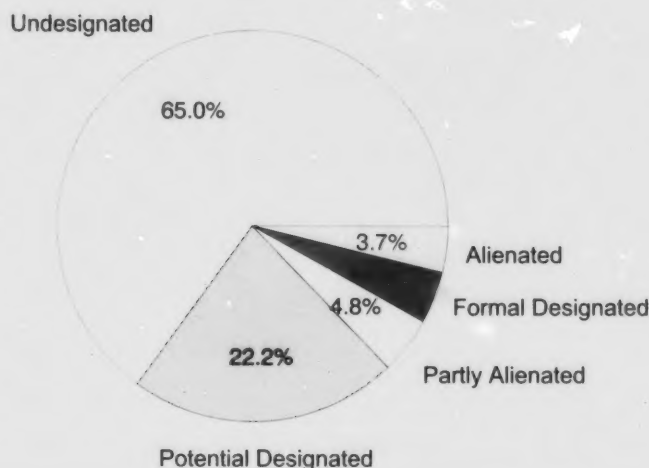
- **Formally Designated Land** is land set aside for a particular purpose which prohibits or limits the use of this land by the public. These lands include such areas as parks, reserves, and archaeological sites and are established pursuant to statutes or Cabinet decisions.
- **Potential Designated Land** is land identified for proposed wilderness reserves and parks, and proposed land claim settlement areas.
- **Alienated Land** is land which includes private land, mining leases, hydro corridors and special development areas.
- **Partly Alienated Land** is land where timber rights are held are defined as partly alienated lands. These other types of lands are established under the general authority and responsibility of departments that manage the resources and developments concerned.
- **Undesignated Land** includes all other land which is not classified into one of the four previous categories.

Figure 3 provides information on the extent of the various types of land designations in the Province.

### 3.26 Management of Crown Land

Figure 3

#### Land Designations



Source: Land Base Statistics (1994), Department of Government Services and Lands

As shown in Figure 3, approximately 65% of the land in the Province is classified as undesignated. Once waterbodies and wetlands are considered, which may not be suitable for development, it is estimated that 43% of Province's land mass is not subject to any restrictions.

There are numerous Government departments and agencies that manage resources or conduct activities that affect the use of land in the Province including Crown land management, resource management, urban and rural planning, facilities and infrastructure development and regional economic development. Comprehensive land use policies are necessary to achieve a co-ordinated approach for land use that minimizes land use conflicts among these departments and agencies and ensures consistency with Government's social, economic, and environmental objectives.

Our review of land use planning indicated that there is no approved stated land use policy and there is no co-ordinated and authoritative approach within Government for land use. We also determined that current planning within the Department is mainly limited to a three year plan for recreational cottage lot development and these plans cover only small areas of the Province. Our review also indicated that other departments responsible for the management of resources and activities that affect the

### 3.26 Management of Crown Land

use of land continue to conduct their planning mainly in isolation of one another.

A mechanism does exist, however, with the mandate to improve the co-ordination of land use within Government in the form of the Interdepartmental Land Use Committee (ILUC). This Committee was established by Government in 1983 and consists of representatives from the various Government departments and agencies which are responsible for resources and activities that significantly affect land planning and management. The Committee reviews land use proposals excluding individual Crown land applications. An Interdepartmental Review Committee which was established by a Committee of Cabinet in 1993, however, concluded that although the ILUC is effective in identifying resource and land use conflicts and in devising means of resolving those conflicts at an operational level, it did not have the authoritative mandate to bring forward land use policy issues for consideration at the executive and political levels.

The terms of reference for the 1993 Committee were to establish an approach for the development of a comprehensive land use policy framework for the Province and to identify a specific administrative mechanism to achieve enhanced coordination and integration of land use planning activity and decision-making within Government. The Report was completed in 1994.

In October of 1994 Cabinet approved, in principle, the recommendations included in the report and directed that plans for implementing the report's recommendations be reported back to Cabinet, that the Department coordinate all aspects of the implementation of the recommendations in the report, and that the Department and Treasury Board identify the additional financial and human resources necessary to implement the recommendations. In 1997, the Department initiated a special project to develop an implementation plan for the recommendations identified in the report. A summary of the Land Use Policies used by the various departments was prepared in March of 1999 and this initiative is now the responsibility of the Lands Management Division.

As the Province still does not have comprehensive land use policies to facilitate a co-ordinated approach for land use within Government, planning for land use within Government is fragmented and covers only small areas of the Province. Discussion with Departmental officials indicated that a comprehensive land plan for the entire Province is not practical due to the significant costs involved. However, it would be prudent for Government to complete comprehensive land plans for certain areas of the Province including those areas where potential for conflict over land use exists.



### 3.26 Management of Crown Land

**Figure 4**

**Crown Land Titles  
31 March 1999**

| Type of Title        | Number       |
|----------------------|--------------|
| <b>Leases:</b>       |              |
| Recreational Cottage | 231          |
| Residential          | 61           |
| Commercial           | 63           |
| Agriculture          | 55           |
| Other                | <u>44</u>    |
|                      | <b>554</b>   |
| <b>Licences:</b>     |              |
| Remote Cottage       | 1,052        |
| Other                | <u>416</u>   |
|                      | <b>1,468</b> |
| <b>Grants</b> *      | <b>378</b>   |
| <b>TOTAL</b>         | <b>2,400</b> |

Source: Crown Titles System, Department of Government Services and Lands

\* Prior to the new pricing policy

#### **Disposition of Crown Lands**

Under the *Lands Act* the Minister may issue licences, leases and grants to persons interested in acquiring Crown land for specific purposes. On an annual basis, approximately 2,400 titles are issued for the various types of licences, leases and grants. Figure 4 outlines details of these 2,400 titles for 1998-99.

We reviewed the procedures for processing applications to determine whether Crown land is disposed of in accordance with legislation and Departmental policies and to assess whether applications are being processed on a timely basis. We also checked to determine whether the Department had a process in place to ensure appropriate rates are assessed for the disposition of this land. Our review of these areas indicated the following:

### **3.26 Management of Crown Land**

#### **1. Application Processing**

Our review, which included a sample of 22 applications for the use of Crown land indicated that, in general, applications are being processed in accordance with legislation and Departmental policy. This encompassed ensuring that necessary procedures in application processing were completed within required time frames and all required information was on file and applications were properly approved.

In examining these 22 applications, we also reviewed the information maintained in the Application Tracking System which is used to track the progress of individual applications for Crown land from the time the application is received by Government to the time the Crown Titles Document is issued. Our testing of this system indicated that the recorded date in the system indicating when certain procedures were completed in the application process were not accurate. As information entered into this system is not always accurate, it reduces the usefulness of the system for monitoring the status of applications.

We also discussed the use of this system with Regional staff who indicated that they do not generally review the reports available from the system to monitor applications nor do they generally monitor the status of applications. We also determined through discussions with the Regional staff that although there is a referral manual to provide guidance when deciding which Government departments and agencies to refer an application to for input, this manual was developed in 1981 and does not reflect the many organizational changes throughout Government since that time. As a result, regional staff indicate that much of the referral process is through their knowledge of the process and informal understandings that have been developed over the years with other departments and agencies on referring applications. This may result in the inconsistent processing of applications among the various Regional Offices.

We also reviewed a recent Departmental report on the Crowns Land Division which recognized a number of factors that contributed to delays in processing applications for the disposition of Crown land. These factors included a cumbersome review process within the Department with respect to land surveys, a lengthy process for the transfer of applications and documents from the Government Service Centres, where applications are received, to the Regional Lands Offices where applications are processed, and a necessity for applications to be referred to other departments and agencies for their input. This review recommended a number of actions that the Department could take to address these concerns including that the Department undertake a review of the present referral system. This review on the referral system was

### 3.26 Management of Crown Land

completed and a final report prepared in November of 1999. The Department is still in the process of reviewing and validating the findings in this report.

Our review of a sample of 15 approved applications indicated that application processing times, from the initial registration of an application to the issuance of land title, averaged 619 days of which 262 was attributed to the time the applicant takes in returning required information to the Department and 357 days was attributed to the Department's processes. Of the 357 days required by the Department to process the applications, 117 days related to the period it took to receive responses from the referral departments and agencies.

#### 2. New Market Value Pricing System

Prior to 1996, the public could obtain a lease to occupy Crown land at an established annual rate but normally title to the land remained with Government. In 1996 Cabinet authorized the Minister of Government Services and Lands to lease Crown land, with the exception of certain lands, at 20% of the land value as determined by the Department over a five year period with title to transfer to the lessee after the five years. Cabinet also authorized the Minister to offer Crown lands to private developers based on fair market value. The 1996 Budget Speech indicated that the move to this new Market Value Pricing System, as well as a fee increase, would generate approximately \$6.2 million in additional revenue for 1996/97. The Department projected additional revenues for the five years ending 31 March 2001 at \$15 million. Figure 5 provides information on these revenue projections giving effect for the new pricing policy for the five years from 31 March 1997 to 31 March 2001 and the actual revenues received.

Figure 5

#### Revenue Projections 31 March

|                                      | 1997      | 1998    | 1999    | 2000    | 2001    |
|--------------------------------------|-----------|---------|---------|---------|---------|
| Revenue estimate- new pricing policy | \$8,860   | \$7,780 | \$4,300 | \$4,380 | \$4,450 |
| Revenue estimate - old policy        | 2,640     | 2,800   | 2,950   | 3,110   | 3,260   |
| Incremental revenue                  | 6,220     | 4,980   | 1,350   | 1,270   | 1,190   |
| Actual revenue                       | 7,135     | 8,333   | 4,142   | n/a     | n/a     |
| Above (below) estimate               | (\$1,725) | \$553   | (\$158) | n/a     | n/a     |

Source: Government Services and Lands 1996 Budget Submission

n/a - not available



### 3.26 Management of Crown Land

completed and a final report prepared in November of 1999. The Department is still in the process of reviewing and validating the findings in this report.

Our review of a sample of 15 approved applications indicated that application processing times, from the initial registration of an application to the issuance of land title, averaged 619 days of which 262 was attributed to the time the applicant takes in returning required information to the Department and 357 days was attributed to the Department's processes. Of the 357 days required by the Department to process the applications, 117 days related to the period it took to receive responses from the referral departments and agencies.

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| Above (below) estimate               | (\$1,725) | \$553   | (\$158) | n/a     | n/a     |

Source: Government Services and Lands 1996 Budget Submission  
n/a - not available



### 3.26 Management of Crown Land

Thus, for the three years ended 31 March 1997 to 1999, actual revenue received has approximated revenue estimates under the new Market Value Pricing System.

In response to this new pricing policy, the Department commenced a process of reviewing all existing leases as the lease term expires with a view to converting these leases to grants within the next five to ten years. The Department established a pricing policy for residential leases for \$1,500 a lot, and recreational cottage leases for \$2,500 a lot or \$3,000 for a waterfront lot. Lessees had to avail of this option by October of 1996 or after this date the lessee would be required to pay fair market value. Fair market values were determined based on such factors as selling of nearby properties and professional independent appraisals conducted mainly by the Municipal Assessment Agency and Departmental staff.

Commercial leases are sold for the assessed market value. As with recreational leases, the lessee pays the fair market value of the land over a five year period at which time title to the land transfers to the lessee. Since the new pricing policy came into effect in 1996, a total of 177 commercial leases have been issued. Commercial leases which exceed 20 hectares must be referred to Cabinet for approval. There have been 6 commercial leases of this type since 1996 all of which were approved by Cabinet.

To ensure Crown land was disposed of at a fair value, we reviewed the process used by the Department for determining lease rates. Our review of this area indicated the following:

- We selected a sample of 30 dispositions of Crown land (9 commercial, 21 recreational) to determine whether there was support for the assessed value. Our review indicated that for the sample selected, adequate information, in the form of appraisals performed either by the Municipal Assessment Agency or by Departmental staff, was available to support the fair market value assessed on the property.
- During the first several years there was a significant number of re-assessments conducted as a result of complaints from the applicants regarding the assessed market value. The Department hired a full-time Manager of Market Pricing to conduct re-appraisals when requested by applicants and establish assessments for on-going land developments.
- At the same time applications are sent to referral agencies, they are forwarded to the Municipal Assessment Agency for assessment of the fair market value of the land in question. The Agency charges the Department a fee of \$125 for each assessment. During 1998, 40 of the applications were subsequently turned down by the Lands Branch but the Department had already paid the Municipal



### 3.26 Management of Crown Land

Assessment Agency approximately \$4,000 in assessment fees for these applications.

#### 3. Cottage Lot Development

The Department has also developed several recreational cottage lot areas since 1996. We were informed that pricing policies for recreational cottage lots are established at fair market value with a minimum price of \$2,500 a lot or \$3,000 for a waterfront lot plus development costs. The Lands Division could not readily provide us with a listing of cottage lot developments with the number of developed lots, status of lots, associated costs and revenues. However, after significant effort by Lands Division staff, such a listing was prepared as outlined in Figure 6.

**Figure 6**

#### Expenditures and Revenue Cottage Lot Developments 31 March 1996 - 1999

| Project                  | # Lots     | Inventory remaining | Total costs      | Revenues              |                          |                    | Net Revenue (Expenditure) |                    |
|--------------------------|------------|---------------------|------------------|-----------------------|--------------------------|--------------------|---------------------------|--------------------|
|                          |            |                     |                  | Cash Received to date | Projected future revenue | Total revenue      | To Date                   | Projected Total    |
| Hell Hill                | 36         | 10                  | \$55,425         | \$52,000              | \$128,000                | \$180,000          | (\$3,425)                 | \$124,575          |
| Salmonier Line           | 10         | -                   | -                | 22,400                | 33,600                   | 56,000             | 22,400                    | 56,000             |
| Sandy Point              | 12         | 9                   | 20,171           | 24,000                | 58,500                   | 82,500             | 3,829                     | 62,329             |
| Three Island Pond        | 5          | 1                   | 4,045            | 128,000               | 32,000                   | 160,000            | 123,955                   | 155,955            |
| South Side Road          | 12         | -                   | 290              | -                     | -                        | -                  | (290)                     | * (290)            |
| Paul's Lake Phase I      | 12         | -                   | 23,382           | 54,000                | -                        | 54,000             | 30,618                    | 30,618             |
| Avalon Peninsular Infill | 53         | 24                  | -                | 189,000               | 155,500                  | 344,500            | 189,000                   | 344,500            |
| Garnish Pond             | 13         | 13                  | 14,020           | -                     | 46,800                   | 46,800             | (14,020)                  | 32,780             |
| Raft Pond (Phase II)     | 13         | 13                  | 5,010            | -                     | 52,000                   | 52,000             | (5,010)                   | 46,990             |
| Placentia Junction       | 33         | 33                  | 35,219           | -                     | 165,000                  | 165,000            | (35,219)                  | 129,781            |
| Goose Arm Pond           | 17         | 17                  | 7,908            | -                     | 76,500                   | 76,500             | (7,908)                   | 68,592             |
| Crabb's River            | 87         | 87                  | 400              | -                     | 32,625                   | 32,625             | (400)                     | 32,225             |
| Stagg Pond               | 15         | 15                  | 29,646           | -                     | 75,000                   | 75,000             | (29,646)                  | 45,354             |
| Groves Point Road        | 4          | 4                   | -                | -                     | 10,000                   | 10,000             | -                         | 10,000             |
| Sandy Lake               | 89         | 25                  | 128,306          | 82,800                | 477,700                  | 560,500            | (45,506)                  | 432,194            |
| <b>Total</b>             | <b>411</b> | <b>251</b>          | <b>\$323,822</b> | <b>\$552,200</b>      | <b>\$1,343,225</b>       | <b>\$1,895,425</b> | <b>\$228,378</b>          | <b>\$1,571,603</b> |

Source: Department of Government Services and Lands

\* appraised at \$160,000; Cabinet authorized sale to Habitat for Humanity at \$1



## 3.26 Management of Crown Land

Assessment Agency approximately \$4,000 in assessment fees for these applications.

### 3. Cottage Lot Development

The Department has also developed several recreational cottage lot areas since 1996. We were informed that pricing policies for recreational cottage lots are established at fair market value with a minimum price of \$2,500 a lot or \$3,000 for a waterfront lot plus development costs. The Lands Division could not readily provide us with a listing of cottage lot developments with the number of developed lots, status of lots, associated costs and revenues. However, after significant effort by Lands Division staff, such a listing was prepared as outlined in Figure 6.

Figure 6

#### Expenditures and Revenue Cottage Lot Developments 31 March 1996 - 1999

| Project                  | # Lots     | Inventory remaining | Total costs      | Revenues              |                          |                    | Net Revenue (Expenditure) |                    |
|--------------------------|------------|---------------------|------------------|-----------------------|--------------------------|--------------------|---------------------------|--------------------|
|                          |            |                     |                  | Cash Received to date | Projected future revenue | Total revenue      | To Date                   | Projected Total    |
| Hell Hill                | 36         | 10                  | \$55,425         | \$52,000              | \$128,000                | \$180,000          | (\$3,425)                 | \$124,575          |
| Salmonier Line           | 10         | -                   | -                | 22,400                | 33,600                   | 56,000             | 22,400                    | 56,000             |
| Sandy Point              | 12         | 9                   | 20,171           | 24,000                | 58,500                   | 82,500             | 3,829                     | 62,329             |
| Three Island Pond        | 5          | 1                   | 4,045            | 128,000               | 32,000                   | 160,000            | 123,955                   | 155,955            |
| South Side Road          | 12         | -                   | 290              | -                     | -                        | -                  | (290)                     | *(290)             |
| Paul's Lake Phase I      | 12         | -                   | 23,382           | 54,000                | -                        | 54,000             | 30,618                    | 30,618             |
| Avalon Peninsular Infill | 53         | 24                  | -                | 189,000               | 155,500                  | 344,500            | 189,000                   | 344,500            |
| Garnish Pond             | 13         | 13                  | 14,020           | -                     | 46,800                   | 46,800             | (14,020)                  | 32,780             |
| Raft Pond (Phase II)     | 13         | 13                  | 5,010            | -                     | 52,000                   | 52,000             | (5,010)                   | 46,990             |
| Placentia Junction       | 33         | 33                  | 35,219           | -                     | 165,000                  | 165,000            | (35,219)                  | 129,781            |
| Goose Arm Pond           | 17         | 17                  | 7,908            | -                     | 76,500                   | 76,500             | (7,908)                   | 68,592             |
| Crabb's River            | 87         | 87                  | 400              | -                     | 32,625                   | 32,625             | (400)                     | 32,225             |
| Stagg Pond               | 15         | 15                  | 29,646           | -                     | 75,000                   | 75,000             | (29,646)                  | 45,354             |
| Groves Point Road        | 4          | 4                   | -                | -                     | 10,000                   | 10,000             | -                         | 10,000             |
| Sandy Lake               | 89         | 25                  | 128,306          | 82,800                | 477,700                  | 560,500            | (45,506)                  | 432,194            |
| <b>Total</b>             | <b>411</b> | <b>251</b>          | <b>\$323,822</b> | <b>\$552,200</b>      | <b>\$1,343,225</b>       | <b>\$1,895,425</b> | <b>\$228,378</b>          | <b>\$1,571,603</b> |

Source: Department of Government Services and Lands

\* appraised at \$160,000; Cabinet authorized sale to Habitat for Humanity at \$1

### 3.26 Management of Crown Land

Our review of this area indicated the following:

- We selected 3 of the 15 above projects to assess the accuracy of recorded costs and revenues and for all 3 of these samples the reported costs were not accurate and did not include salary costs associated with personnel who are involved in the development of cottage lots. In addition, the cost as determined by the Department does not agree with the cost reported in the financial statements of the Province.
- The Department does not maintain, on a Province-wide basis, an on-going record of cottage lot developments indicating the number of developed lots, the number of lots unsold, associated costs and revenues. On a regional basis, information about sold and unsold lots is available.
- Overall, the Land Management Division does not maintain adequate information on cottage lot developments, including the status of the developments and the associated costs and revenues. Accurate, complete and comprehensive information on status of lot sales and the associated costs and revenues would enhance information available to Management for the monitoring of existing developments and the planning of future developments.

#### 4. Leases to EDGE Companies

To attract investment to the Province, the Government, under the *Economic Diversification and Growth Enterprises Act*, provides significant tax and other incentives to new and expanding corporations that meet a number of qualifying criteria. EDGE companies must continue to meet these qualifying criteria or their status as an EDGE company can be revoked along with all the various incentives. One incentive that is offered to EDGE companies is the ability to lease unserviced industrial lots at \$1. Our review of this area indicated the following:

- Although Departmental officials indicated that a number of EDGE companies had leased Crown land at \$1, they could not provide us with any information regarding which EDGE companies had leased this land, what land had been leased, or what the land was being used for. Discussion with officials at the Department of Industry, Trade and Technology, who are responsible for administering the EDGE program, also were aware that there were a number of EDGE companies that leased Crown land for \$1. However, again these officials could not provide us with any information on the names of these companies, where the land was

### **3.26 Management of Crown Land**

situated, or what the land was being used for. Thus, there has been no monitoring by the Department regarding the status of this land or whether these companies still have eligible EDGE status.

- We therefore requested the Department to develop a list of EDGE companies that are leasing Crown land at \$1 and after significant effort by the Department, a listing was provided to us. A comparison of this list with those EDGE companies that have had their status revoked indicated that all of the companies that are leasing Crown land for \$1 still have EDGE status.
- There is nothing in the agreements between Government and EDGE companies to address what would happen to this land if the company lost its EDGE status.

### **5. Illegal Occupation of Crown Lands**

The *Lands Act* provides that persons wrongfully in possession of Crown lands shall deliver up the lands to the Crown and those persons may be subject to imposed fines. Discussion with Departmental officials indicated that upon becoming aware of a case of illegal occupancy, the Department will determine whether there had been any "freeze" on development in the area as imposed by the Department. If it is established that there was no "freeze" on development in the area, the Department does not remove the illegal dwelling rather it imposes fines upon the person and requires the person to register the land with the Department and pay the required lease rates. However, if the Department determines that the occupant built a dwelling after a "freeze" on development was in force, Department officials indicate that the occupant is asked to remove the dwelling from the land or the dwelling is forcibly removed by the Department.

We also determined that even in areas where cottage lots are being developed and a public draw is being held, illegal occupants in this area who built a dwelling before a "freeze" on development was imposed by the Department, are assessed an illegal occupation fee and required to pay the fair market value as determined by the Department. This process removes this parcel of land from the public draw and as a result, the public never has access to this previous illegally occupied Crown land.

### **Management of Crown land leases, licences and grants**

The Department manages approximately 62,000 Crown land leases, licences and grants as outlined in Figure 7.





### 3.26 Management of Crown Land

**Figure 7**

#### **Types of Crown Land Dispositions**

| Type of Land Disposition | Number        |
|--------------------------|---------------|
| Leases                   | 10,533        |
| Licences                 | 11,593        |
| Grants                   | 39,771        |
| <b>Total</b>             | <b>61,897</b> |

Source: Department of Government and Lands Crown Titles System, October 1999

To effectively manage this area, an inventory of these leases, licences and grants must be accurately maintained and updated, monitoring procedures must exist to ensure that the land is being used for its intended purpose, and appropriate billing and collection procedures must be in place. Our review of these areas indicated the following:

#### **1. Inventory of Leases, Licences and Grants**

A listing of registered Crown land leases, licences and grants is available through the Department's Crown Titles System. Our review of 67 approved land applications indicated that as these licences, leases and grants were approved, they were accurately updated to the Crown Titles System.

#### **2. Monitoring of Crown Land Utilization**

Adequate monitoring procedures must be in place to ensure that an applicant is fulfilling the terms of the lease with respect to required development and how the land was intended to be used. To assist in monitoring the terms of these leases, reports are produced from the Department's Application Tracking System which indicate those leases where development of the land was required to be completed.

### 3.26 Management of Crown Land

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### **3.26 Management of Crown Land**

Our review of this area indicated that for the lands where development should have occurred, very few physical inspections of these sites are conducted. Unless a complaint is received from the public on a particular parcel of Crown land, monitoring procedures are limited to sending out affidavits to individuals, after five years have lapsed, which the individual completes to attest to the fact that the terms of the lease, licence or grant have been adhered to. Discussion with Regional Offices indicated that affidavits are not always sent out when required. As a result, the Department cannot determine whether Crown land is being used for the purposes intended when the land was authorized for disposition.

#### **3. Billing and Collection of Fees**

Once a lease, licence or grant for Crown land is issued, adequate procedures should be in place to ensure that assessed fees are issued and collected on a timely basis. The billing and collection of fees is the responsibility of the Department of Municipal and Provincial Affairs.

We reviewed a sample of 26 leases to determine whether billings were properly prepared and recorded in the accounting records, and whether lease rates were reviewed by the Department at the renewal of a lease to ensure that rates were adjusted where appropriate. Our review indicated the following:

- For those leases where title to the land will be transferred to the lessee after the lease is paid off over 5 years, the Department has only recorded the current portion or 1/5 of the balance owing in the accounting records. As a result, while the Department has estimated how much money is due and payable, the amount which is not yet due, and which we estimate to be very significant, is not yet known by the Department.
- The accounts receivable at 31 March 1999 as per the Department's records indicate that \$2,436,130 or 89% of the \$2,739,712 is overdue. Figure 8 outlines the detailed ageing of the receivables at 31 March 1999.

### 3.26 Management of Crown Land

Figure 8

**Accounts Receivable**  
**31 March 1999**

| Ageing Category              | Amount               |
|------------------------------|----------------------|
| Less than 30 days            | \$303,582            |
| Between 30 days and 90 days  | 290,773              |
| Between 91 days and 365 days | 820,626              |
| Greater than 365 days        | 1,324,731            |
| <b>Subtotal</b>              | <b>2,739,712</b>     |
| Amount not yet due           | Not Available        |
| <b>Total</b>                 | <b>Not Available</b> |

Source: Department of Government Services and Lands

- When the Department of Government Services and Lands had the responsibility for the collection of accounts, there were collection policies specific to these types of fees. The accounts receivable clerks at the Department of Municipal and Provincial Affairs were not aware of these policies and indicated that they follow the collection procedures as outlined in the Government's Management Manual. However, our review indicated that there is no regular collection activity performed by the Department of Municipal and Provincial Affairs.
- With the exception of the preparation of the quarterly ageing report that is required to be submitted to Treasury Board, accounts receivable are not monitored by either accounts receivable clerks at the Department of Municipal and Provincial Affairs or Crown lands officers.
- There is very limited communication between accounts receivable clerks at the Department of Municipal and Provincial Affairs and staff who administer leases in the Crown lands branch unless it relates to an account where an individual is making a request with respect to the land and the fees are still outstanding. Therefore, Crown lands staff are not always aware of any problem accounts

### 3.26 Management of Crown Land

for which they may wish to consider conducting a site inspection or making contact with the lessee if they are in that particular area.

- The accounts receivable report is 334 pages long and includes 11,000 accounts. These accounts are not presented in any type of order and a cursory review of the report indicates several lessees/purchasers have several accounts. In addition, the report does not show the receivables by category (e.g. lease or licence). As a result, the report is not very informative and is difficult to review.

As a result, the Department does not have sufficient information to adequately manage its accounts receivable.

We reviewed a sample of 58 billings for land grants (ie. title to the land is transferred to the purchaser) to determine whether they were properly prepared. In accordance with the new Market Value Pricing System, in preparing final billings for land grants, where applicable, the Department reduced the assessed sales price by any previous lease payments on the land by the purchaser. Our review indicated that in 5 instances, as a result of inaccurate information in the accounts receivable system on previous years' lease payments, although the assessed sales price was accurately determined, the Department did not deduct the correct amount of previous lease payments on the land. As a result, these 5 individuals paid the incorrect amount for title to the land; however, the amounts were not significant.

#### 4. Geographic Information Systems

An emerging trend in the management of natural resources is the development of geographic information systems (GIS). GIS refers to computer systems designed to allow users to collect, manage and analyze large volumes of data related to geographically referenced data and information. The development of a GIS for this Province has been hampered by a number of factors. For example, while land use information is available, it resides in a wide variety of systems maintained by different departments and the systems are not able to interface or integrate with one another without considerable technical support. In addition, thematic layers indicating land ownership have not been produced for all areas of the Province, some of the existing base maps are out of date, and base mapping and the Crowns Titles layer at the scale of 1:2,500 for use in GIS applications is not complete for the whole Province.



### 3.26 Management of Crown Land

In February of 1997, the Department of Government Services and Lands and the Department of Environment and Labour submitted to Cabinet a proposed Geomatics Strategy for the Province. The report indicated that other Government departments and agencies have developed or are in the process of developing comprehensive georeferenced data bases, geographic information systems and applications largely in isolation of each other which could result in significant duplication of effort and numerous problems due to incompatible data and standards. The report stressed that the development and general acceptance of data standards is the most critical element in the development of a GIS. At this time, Cabinet approved this strategy in principle with final approval held until an implementation plan was submitted to Cabinet for consideration within six months or August of 1997. Our review indicated that the Department has yet to report back to Cabinet. The Department informed us that the development of an implementation plan is still ongoing.

The Lands Branch has converted the base maps and several of its land management thematic layers including the Crown Titles System and Land Use Atlas into digital format for use in GIS applications. However, these developments have been completed without an approved Provincial Geomatics Strategy being in place. In addition, the Crown Titles System that was converted contained incomplete and outdated information and as a result, the new digitized version is also incomplete and outdated.

#### Recommendations

*The Department should continue efforts to develop a complete land parcel identification system to establish the extent and boundaries of Crown lands.*

*The Department should continue efforts to develop comprehensive land use policies to facilitate a co-ordinated approach for land use within Government. The Department should also review the merits of undertaking more comprehensive land planning in the Province.*

*The Department should continue efforts to both improve the efficiency of the application process and to improve the accuracy of data in the Application Tracking System with which to monitor the status of applications.*

*The referral to the Municipal Assessment Agency should be delayed until the Regional Lands Office approves the application.*

*The Department should maintain a complete listing of any EDGE companies that are leasing Crown land for \$1 and actively monitor these leases to ensure that the land is being used as intended and the company maintains its EDGE status.*



### **3.26 Management of Crown Land**

*Leases between Government and EDGE companies should contain a clause that provides for a change in the lease rate to fair value if the company loses its EDGE status.*

*The Department should review its monitoring procedures over land use.*

*As revenue from leases assists in covering costs of managing Crown lands, the Department should participate in the monitoring of the accounts receivable.*

*The Department should continue its involvement in the development of a both a Geomatics Strategy for the Province and Geographic Information System applications.*

#### **Department's Response**

##### ***Identification and Use of Crown Lands***

*The Lands Branch's mandate pertains to the management of Crown lands only.*

*To change the current system of land registration and title validation in the Province to a guaranteed land title system would be an extremely expensive process costing millions of dollars, that would take years to complete. The current system does not impose unmanageable impediments to the management of Crown land and land ownership disputes between the Crown and claimants of Crown land are dealt with as they arise.*

*The continuing development of a Crown land parcel identification system is a key component of the Department's Crown Land Geographic Information System (GIS). Improvements will continue to be made to enhance the integrity and accuracy of the data base which in turn strengthens our information regarding the extent and location of Crown lands.*

*Because of the extensive number of legally valid but unregistered land claims by adverse possession (squatters' rights) in the province, the determination of the boundaries of all Crown land parcels will be difficult to achieve in a short time frame. However as claims are settled under the Lands Act and the Quieting of Titles Act on an ongoing basis, the resulting boundary locations are continually being added to the Crown's mapping.*

### **3.26 Management of Crown Land**

#### ***Land Use Policy and Planning***

*The Department agrees that it should continue to develop land use policies to facilitate a co-ordinated approach for land use within Government. The Department in 1996 initiated a project to draft provincial land use policies. This project is partially complete and is scheduled for completion in 2000.*

*The Department is in the process of responding to the recommendation in the Report of the Committee of Ministers and Members of the House of Assembly on the Use of Outdoor Resources, which directed the Department to:*

*review its land use policy with the intention of placing a priority on developing land use plans for areas of high user conflict.*

*The Department is also taking action to revitalize the Interdepartmental Land Use Committee and to reorganize the Land Management Division to enhance its ability to coordinate land use policies.*

#### ***Application Processing and Market Value Pricing***

*The Department is pleased that the Auditor General has confirmed that the Department processes applications and establishes values for land sales for Crown lands as specified by legislation and Department policy.*

*The Department continues to take initiatives to improve the efficiency of the application process and has completed two major reviews during the past year with the objective of improving processing times and the accuracy of data. The first review identified insufficient human resources in the Regional Offices to accomplish the mandated duties. Government has recognized this and six new positions have been approved and are currently in the process of being filled.*

*The second review addressed the system of interdepartmental referrals that are made on applications. Delays in this process are being addressed with the development of interdepartmental protocols whereby the departments and agencies involved in the decision making process have agreed to limit response times. The Department in turn, through its Strategic Planning process, has identified the establishment of new procedural guidelines for the monitoring of applications contained within the ATS and to ensure routine reviews of active applications are made on a consistent basis. This will include scheduled reviews and reporting on a monthly and bi-monthly basis.*

### **3.26 Management of Crown Land**

*A recent review of the ATS also indicates improvements can be made by utilizing the new Application Management System currently in use within the Department. This will provide improved processing, monitoring and reporting functions.*

#### ***Municipal Assessment Agency***

*The Department is restructuring the procedure for submitting referrals on land valuation to the Municipal Assessment Agency. The valuation will be assigned only after the application has received final approval. This will reduce needless expenditures for valuations on applications that cannot be approved, but will necessarily lengthen the application processing time.*

#### ***Leases to EDGE Companies***

*There are a total of six (6) EDGE companies with Crown land leases.*

*The EDGE leases issued for Crown lands are now compiled and maintained in a separate listing in the Crown Lands Registry. The Department is developing a protocol with the Department of Industry, Trade and Technology to ensure EDGE leases are monitored in order that the Crown Lands Division is aware of any changes that could affect the lease for Crown land.*

*EDGE leases for Crown land currently contain a rent review clause which ensures the annual rent can be reviewed and adjusted at 5 year intervals. An EDGE company which loses its EDGE status will have its annual rent reviewed on a scheduled basis and moved to Government's market value leasing structure. The Department, in conjunction with the Department of Justice, is preparing a new clause for EDGE leases which will ensure that any company that loses its EDGE status will immediately be subject to Government's Market Value Pricing Policy.*

#### ***Management of Crown Land Leases, Licences and Grants***

*The Department is currently reviewing its procedures on monitoring leases to ensure there is compliance with lease conditions. The Land Management Division also has initiated a central, project-specific records system that incorporates all related cottage lot development costs, the number of lots allocated, annual and total lot revenues and a running inventory of the lots still available. This information is maintained in a computer data base in the Land Management Division.*

### **3.26 Management of Crown Land**

#### ***Billing and Collection of Fees***

*The Department has initiated discussions with the Department of Municipal and Provincial Affairs (MAPA) to improve the monitoring and collection of accounts receivable and will begin immediately to monitor these accounts. The Department will also monitor to ensure that a comprehensive collection policy is put in place and explore with MAPA alternate ways of collecting existing outstanding accounts. The Department is pleased that the AG confirmed that no Crown grants are issued without full payment of all rents and fees.*

*The Department of Municipal and Provincial Affairs will review its accounting process for 5 year lease receivables with a view to determining the appropriate treatment of this account.*

*Monitoring of accounts receivables by MAPA is done within existing resources. Special collection initiatives are also undertaken on a periodic basis. MAPA is currently reviewing its collection policies to enhance and strengthen collection procedures in order to ensure the more timely collection of accounts. The new policy will be implemented within the next month.*

*The Department's accounts receivables will be moved to Government's new oracle accounts receivable system within several months. This new system will provide MAPA with more flexibility and options with regard to presentation of these accounts.*

#### ***Geographic Information Systems***

*The Surveys and Mapping Division has been building the digital foundation (base maps) for geomatics for over ten years, and the Crown Lands and Land Management Divisions have been building spatially integrated thematic layers for the past several years in line with the strategy. The Lands Branch is taking the lead in the Provincial Geomatics Strategy, and development of the implementation plan. Both thematic layers are designed to be used on the standard government base map provided by the Survey and Mapping Division which is the foundation data for all government geographic information systems.*

### 3.27 The Western Health Care Corporation

#### Introduction

The Western Health Care Corporation was constituted under the *Hospitals Act Constitution Order*. The Corporation is responsible for the management and control of the operations of acute and long term care facilities in the western region of the province of Newfoundland and Labrador. On 1 January 1996, the Board assumed responsibility for the following facilities:

Western Memorial Regional Hospital and Western Linen Services (Corner Brook);  
Bonne Bay Hospital (Norris Point);  
Dr. J. I. O'Connell Centre (Corner Brook);  
Calder Health Centre (Burgeo);  
Rufus Guinchard Health Care Centre (Port Saunders);  
Bay St. George Senior Citizens Home (Stephenville Crossing);  
Sir Thomas Roddick Hospital (Stephenville);  
Dr. Charles L. Legrow Health Centre (Port aux Basques); and  
Interfaith Home for Senior Citizens (Corner Brook).

In our report to the House of Assembly for the year ended 31 March 1996 we reported on the results of our review of the Western Memorial Hospital Corporation. In 1996, we concluded that the Western Memorial Hospital Corporation had significant weaknesses in all areas reviewed. Specifically, management practices were inadequate with regards to financial monitoring, budgeting, receivable collections, safeguarding of assets, and compliance with legislation. Purchasing practices were inadequate, in that the *Public Tender Act* was not being complied with, personal charges were being applied to corporate credit cards and inventory controls were inadequate. In addition, human resource practices required improvement as competition files were not always maintained, employee benefits were in excess of Government guidelines, performance appraisals were not always performed, and controls over the monitoring and approval of employee leave and overtime were weak.

In September 1997 the Public Accounts Committee held public hearings on the Western Health Care Corporation. At that time we indicated that we would be carrying out an additional review at a later date.

#### Scope and Objectives

We commenced a review of the Western Health Care Corporation in March 1999. The objectives of this review were to assess whether the Corporation had taken adequate steps to address issues identified in our previous review. More specifically, our objectives were to assess whether procedures have been established to ensure:

- the Corporation's financial position is adequately monitored and that key financial systems are operating efficiently;



### 3.27 The Western Health Care Corporation

- financial and physical assets are adequately safeguarded and utilized;
- purchases are adequately monitored and controlled and comply with Corporation policies and the *Public Tender Act* and Regulations; and
- the board is complying with the *Hospitals Act* and government policies particularly in the areas of employee compensation and travel.

#### Conclusions

Since our original review in 1996, the Western Health Care Corporation has made some improvements in the financial management of the Corporation. These include the improved timeliness of year end financial reporting and the reduction in inappropriate expenditures for employee benefits and travel. However, there are areas that need to be addressed as there are still significant weaknesses. These include:

- Although the Corporation has been provided with \$20.9 million in additional funding during 1998-99, there remains a deficit of \$19.4 million as at 31 March 1999. This is comprised of the 1998-99 operating deficit of \$3.1 million, a \$700,000 capital deficit and a \$15.6 million deficit relating to severance pay and annual leave accruals. The \$15.6 million will have to be funded as it becomes due. The additional funding of \$20.9 million was not intended to continue as part of the annual government contribution.

Expenditures continue to increase at a faster rate than Provincial funding. As a result, deficits will continue to occur unless the Corporation reduces expenditures or the Government increases funding. As at the time of our review (November 1999), the Corporation is projecting a deficit of \$15.7 million in 1999-2000 excluding depreciation, severance pay and vacation pay.

- Although patient receivables have declined since our previous review in 1996, the percentage of amounts considered collectable has decreased. In 1995, the Western Regional Memorial Hospital estimated that it would collect \$766,000 or 64% of the \$1.2 million owed to it by former patients. However, in 1999, the Corporation estimates that it will collect \$689,000 or 49% of the \$1.4 million owed to it.
- One particular area of concern is the amount due from employees for travel advances and salary advances. These amounts have been advanced to employees as a part of the normal operations of



### **3.27 The Western Health Care Corporation**

the Corporation; however, the failure to subsequently collect or account for these advances has been a significant weakness.

- Controls over capital assets are not adequate. Capital assets are not physically identified, listed, costed or counted periodically.

Although the Corporation has a computerized database to record maintenance for significant equipment, this database is not kept up to date or monitored to determine which equipment requires maintenance. Maintenance contracts are not listed or monitored to ensure that contracts are renewed as required. As a result, we could not determine whether all equipment is properly maintained.

- The inaccuracies of the computerized inventory records as evidenced by the significant number of differences between the computerized records and the physical counts indicate that controls over inventories need improvement. Our test counts identified variances that could not be reconciled to Corporation records.

#### **Findings and Recommendations**

#### **Financial Management**

##### **1. Financial Position**

The Corporation commenced operations 1 January 1996 and took over the operations of six previously separate boards. These boards transferred to the Corporation on start-up in 1995 a combined bank indebtedness of approximately \$800,000. Since 1995, the Corporation has had difficulty operating within the limits of its annual budgets and as a result the bank loans have increased from \$800,000 in 1995 to \$22.5 million in 1999. Figure 1 outlines the financial position of the Corporation from 1995 to 1999.

### 3.27 The Western Health Care Corporation

Figure 1

**Western Health Care Corporation  
Financial Position - Operating Fund  
31 December 1995 and 31 March 1996-1999  
(\$ Millions)**

|                                  | 1995          | 1996          | 1997          | 1998           | 1999           |
|----------------------------------|---------------|---------------|---------------|----------------|----------------|
| <b>Assets</b>                    |               |               |               |                |                |
| Accounts receivable              | \$ 3.4        | \$ 4.5        | \$ 5.5        | \$ 3.6         | \$ 30.1        |
| Other current assets             | 2.4           | 4.7           | 4.5           | 4.5            | 4.8            |
|                                  | 5.8           | 9.2           | 10.0          | 8.1            | 34.9           |
| Due from associated funds        | 1.3           | 5.7           | 1.5           | 1.5            | 2.2            |
| Capital assets                   | 24.9          | 14.5          | 25.6          | 25.1           | 24.3           |
| Trust funds and other            | 0.5           | 0.3           | 0.4           | 0.3            | 0.4            |
|                                  | \$ 32.5       | \$ 29.7       | \$ 37.5       | \$ 35.0        | \$ 61.8        |
| <b>Liabilities</b>               |               |               |               |                |                |
| <b>Bank indebtedness</b>         | <b>\$ 0.8</b> | <b>\$ 8.1</b> | <b>\$ 9.3</b> | <b>\$ 14.8</b> | <b>\$ 22.5</b> |
| Other current liabilities        | 17.6          | 10.6          | 15.3          | 13.6           | 21.1           |
|                                  | 18.4          | 18.7          | 24.6          | 28.4           | 43.6           |
| Trust liabilities and other      | 0.4           | 0.4           | 0.4           | 0.3            | 0.4            |
| Long term debt                   | 4.4           | 4.3           | 4.8           | 4.7            | 4.6            |
| Deferred contributions - capital | 7.3           | -             | 15.4          | 15.3           | 19.9           |
| Severance pay accrual            | 7.4           | 9.7           | 10.4          | 11.4           | 12.7           |
| Equity                           | (5.4)         | (3.4)         | (18.1)        | (25.1)         | (19.4)         |
|                                  | \$ 32.5       | \$ 29.7       | \$ 37.5       | \$ 35.0        | \$ 61.8        |

Source: Audited financial statements

Financing part of its operations by bank loans is costing the Corporation a significant amount of money. The interest cost for financing its debt in 1998-99 was approximately \$832,000, and approximately \$487,000 in 1997-98. This cost is charged to the Board of Trustees Fund; however, this fund does not have sufficient cash to cover this cost. As a result, the Operating Fund must pay the interest and recover the amount from the Board fund. As at 31 March 1999 the Operating Fund was owed approximately \$2 million by the Board Fund for interest on bank loans.

### 3.27 The Western Health Care Corporation

During the fiscal year 1998-99, the Department of Health provided the Corporation with \$20.9 million in additional funding. Of the \$20.9 million provided, \$5.5 million was paid to reduce the 1998-99 deficit, \$10.6 million was paid to reduce the Corporation's accumulated deficit to 31 March 1998 and \$4.8 million was paid as a cash injection. Figure 2 summarizes the Corporation's deficit as at 31 March 1998, the additional funding provided and the Corporation's deficit as at 31 March 1999.

As indicated in Figure 2 and subsequent to payment of additional deficit funding of \$15.4 million and \$5.5 million by the Department of Health and Community Services, the Corporation continues to carry an accumulated deficit of \$19.4 million as at 31 March 1999. At the time of our review, the Corporation was forecasting a deficit of \$15.7 million, excluding depreciation, severance and vacation pay accruals, for the 1999-2000 fiscal year. If this deficit materializes, the Corporation will have an accumulated deficit of at least \$35.1 million by 31 March 2000.

**Figure 2**

**Western Health Care Corporation  
Impact of Deficit Funding  
Year Ended 31 March 1999  
(\$ Millions)**

|                                | Accumulated<br>Deficit<br>31 March 1998 | Additional<br>Funding<br>Provided | 1999 Operating<br>Results | Accumulated<br>Deficit<br>31 March 1999 |
|--------------------------------|-----------------------------------------|-----------------------------------|---------------------------|-----------------------------------------|
| Vacation and severance accrual | \$ 14.5                                 | \$ 0                              | \$ 1.1                    | \$ 15.6                                 |
| Capital                        | 1.9                                     | (1.9)                             | .7                        | .7                                      |
| Operating                      | 8.7                                     | (8.7)                             | (Note 1) 3.1              | 3.1                                     |
| Total deficit                  | 25.1                                    | (10.6)                            | 4.9                       | 19.4                                    |
| Cash injection                 | -                                       | (4.8)                             | -                         | -                                       |
| <b>Total</b>                   | <b>\$ 25.1</b>                          | <b>\$ (15.4)</b>                  | <b>\$ 4.9</b>             | <b>\$ 19.4</b>                          |

Note 1 - The Corporation's operating deficit of \$3.1 million is after the deficit funding payment of \$5.5 million.  
Source: Audited Financial Statements

### 3.27 The Western Health Care Corporation

Figure 1

**Western Health Care Corporation  
Financial Position - Operating Fund  
31 December 1995 and 31 March 1996-1999  
(\$ Millions)**

|                                  | 1995          | 1996          | 1997          | 1998           | 1999           |
|----------------------------------|---------------|---------------|---------------|----------------|----------------|
| <b>Assets</b>                    |               |               |               |                |                |
| Accounts receivable              | \$ 3.4        | \$ 4.5        | \$ 5.5        | \$ 3.6         | \$ 30.1        |
| Other current assets             | 2.4           | 4.7           | 4.5           | 4.5            | 4.8            |
|                                  | 5.8           | 9.2           | 10.0          | 8.1            | 34.9           |
| Due from associated funds        | 1.3           | 5.7           | 1.5           | 1.5            | 2.2            |
| Capital assets                   | 24.9          | 14.5          | 25.6          | 25.1           | 24.3           |
| Trust funds and other            | 0.5           | 0.3           | 0.4           | 0.3            | 0.4            |
|                                  | \$ 32.5       | \$ 29.7       | \$ 37.5       | \$ 35.0        | \$ 61.8        |
| <b>Liabilities</b>               |               |               |               |                |                |
| <b>Bank indebtedness</b>         | <b>\$ 0.8</b> | <b>\$ 8.1</b> | <b>\$ 9.3</b> | <b>\$ 14.8</b> | <b>\$ 22.5</b> |
| Other current liabilities        | 17.6          | 10.6          | 15.3          | 13.6           | 21.1           |
|                                  | 18.4          | 18.7          | 24.6          | 28.4           | 43.6           |
| Trust liabilities and other      | 0.4           | 0.4           | 0.4           | 0.3            | 0.4            |
| Long term debt                   | 4.4           | 4.3           | 4.8           | 4.7            | 4.6            |
| Deferred contributions - capital | 7.3           | -             | 15.4          | 15.3           | 19.9           |
| Severance pay accrual            | 7.4           | 9.7           | 10.4          | 11.4           | 12.7           |
| Equity                           | (5.4)         | (3.4)         | (18.1)        | (25.1)         | (19.4)         |
|                                  | \$ 32.5       | \$ 29.7       | \$ 37.5       | \$ 35.0        | \$ 61.8        |

Source: Audited financial statements

Financing part of its operations by bank loans is costing the Corporation a significant amount of money. The interest cost for financing its debt in 1998-99 was approximately \$832,000, and approximately \$487,000 in 1997-98. This cost is charged to the Board of Trustees Fund; however, this fund does not have sufficient cash to cover this cost. As a result, the Operating Fund must pay the interest and recover the amount from the Board fund. As at 31 March 1999 the Operating Fund was owed approximately \$2 million by the Board Fund for interest on bank loans.

### 3.27 The Western Health Care Corporation

During the fiscal year 1998-99, the Department of Health provided the Corporation with \$20.9 million in additional funding. Of the \$20.9 million provided, \$5.5 million was paid to reduce the 1998-99 deficit, \$10.6 million was paid to reduce the Corporation's accumulated deficit to 31 March 1998 and \$4.8 million was paid as a cash injection. Figure 2 summarizes the Corporation's deficit as at 31 March 1998, the additional funding provided and the Corporation's deficit as at 31 March 1999.

As indicated in Figure 2 and subsequent to payment of additional deficit funding of \$15.4 million and \$5.5 million by the Department of Health and Community Services, the Corporation continues to carry an accumulated deficit of \$19.4 million as at 31 March 1999. At the time of our review, the Corporation was forecasting a deficit of \$15.7 million, excluding depreciation, severance and vacation pay accruals, for the 1999-2000 fiscal year. If this deficit materializes, the Corporation will have an accumulated deficit of at least \$35.1 million by 31 March 2000.

**Figure 2**

**Western Health Care Corporation  
Impact of Deficit Funding  
Year Ended 31 March 1999  
(\$ Millions)**

|                                | Accumulated<br>Deficit <sup>1</sup><br>31 March 1998 | Additional<br>Funding<br>Provided | 1999 Operating<br>Results | Accumulated<br>Deficit<br>31 March 1999 |
|--------------------------------|------------------------------------------------------|-----------------------------------|---------------------------|-----------------------------------------|
| Vacation and severance accrual | \$ 14.5                                              | \$ 0                              | \$ 1.1                    | \$ 15.6                                 |
| Capital                        | 1.9                                                  | (1.9)                             | .7                        | .7                                      |
| Operating                      | 8.7                                                  | (8.7)                             | (Note 1) 3.1              | 3.1                                     |
| Total deficit                  | 25.1                                                 | (10.6)                            | 4.9                       | 19.4                                    |
| Cash injection                 | -                                                    | (4.8)                             | -                         | -                                       |
| <b>Total</b>                   | <b>\$ 25.1</b>                                       | <b>\$ (15.4)</b>                  | <b>\$ 4.9</b>             | <b>\$ 19.4</b>                          |

Note 1 - The Corporation's operating deficit of \$3.1 million is after the deficit funding payment of \$5.5 million.  
Source: Audited Financial Statements

### 3.27 The Western Health Care Corporation

#### 2. Accounts Receivable

As at 31 March 1999, the Corporation was owed approximately \$31.3 million in accounts receivable with an allowance for doubtful accounts of \$1.2 million and was owed another \$2.2 from associated funds. Of the \$31.3 million in accounts receivable, \$27 million was due from the Province, most of which related to the \$20.9 million in special one-time funding. Of the remaining \$4.3 million, \$1.4 million was due from patients, \$922,000 was due from employees and \$2.0 million related to sundry accounts receivable.

At the time of our previous review in 1996 significant problems were identified in the controlling and monitoring of accounts receivable of the Corporation. These included the use of health care funding of \$4.8 million to finance other funds of the Corporation, inadequate monitoring and controlling of patient receivables, the use of Corporation funds to provide employee loans and the use of Corporation funds for personal expenses. Our current review identified improvements in each of the weaknesses; however, some concerns still exist as follows:

- The amount owed to the Corporation by other funds has been reduced from \$4.8 million as at 31 March 1995 to \$2.2 million as at 31 March 1999. The main reason for the decline is one of the other funds which owed money to the Corporation became part of the Corporation and transferred its assets and liabilities to the operating fund thus eliminating an accounts receivable of \$3.8 million.

Of the \$2.2 million owed by other funds, \$2.1 million is owed by the Board of Trustees Fund. This is an increase over the 31 March 1995 balance of \$1.4 million because government policy requires that the Board of Trustees Fund must cover any overdraft interest charges. These interest charges were approximately \$832,000 in 1998-99. The Board of Trustees Fund does not have any cash to pay this amount or the other \$1.2 million that it owes the Operating Fund. The remaining \$0.1 million is owed by the Western Memorial Hospital Foundation with most of the amount owed for an ambulance purchase.

- Although patient receivables have declined from \$1.7 million in 1995 to \$1.4 million as at 31 March 1999, uncollectible accounts are still a concern. As indicated in Figure 3, doubtful accounts of \$722,538 in 1999 represent 51% of total patient receivables.



### 3.27 The Western Health Care Corporation

Figure 3

#### Western Health Care Corporation Patient Receivables 31 March

| Site                                         | 1999         |            |            | 1995         |            |              |
|----------------------------------------------|--------------|------------|------------|--------------|------------|--------------|
|                                              | Receivable   | Allowance  | Net        | Receivable   | Allowance  | Net          |
| Western Memorial Regional Hospital           | \$ 479,561   | \$ 108,979 | \$ 375,582 | \$ 992,728   | \$ 353,977 | \$ 638,751   |
| Bonne Bay                                    | 19,427       | 15,199     | 4,228      | 22,341       | 153        | 22,188       |
| Dr. J. I. O'Connell Centre                   | 391,043      | 346,308    | 44,735     | 166,024      | 74,697     | 91,327       |
| Calder Health Centre                         | 26,334       | 11,879     | 14,455     | 14,494       | 1,085      | 13,409       |
| Former Western Memorial Hospital Corporation | 916,365      | 477,365    | 439,000    | 1,195,587    | 429,912    | 765,675      |
| Interfaith Home for Senior Citizens          | 121,530      | 103,178    | 18,352     | 4,003        | Note 1     | 4,003        |
| Rufus Quinard Health Centre                  | 28,497       | 23,715     | 4,782      | 4,329        | Note 1     | 4,329        |
| Bay St. George Senior Citizen's Home         | 11,557       | 0          | 11,557     | 15,509       | Note 1     | 15,509       |
| Sir Thomas Roddick Hospital                  | 274,981      | 92,741     | 182,240    | 318,269      | Note 1     | 318,269      |
| Dr. Charles L. Legrow Health Centre          | 58,650       | 25,539     | 33,111     | 165,226      | Note 1     | 165,226      |
|                                              | \$ 1,411,580 | \$ 722,538 | \$ 689,042 | \$ 1,702,923 | \$ 429,912 | \$ 1,273,011 |

Note1: Allowance not available for the entities other than Western Memorial Hospital Corporation at 31 March 1995. Amounts indicated are net of the allowance for doubtful accounts.

Source: Western Health Care Corporation financial records

- A significant issue from our previous review was the extent of financing provided to employees for personal purchases. As at 31 March 1995, \$552,513 was owed to the Corporation's Board Fund for employee loans and \$77,512 was owed to the Operating Fund for payroll, travel and other advances. At 31 March 1999 all but \$46,245 of the \$552,513 had been repaid while another \$34,084 was owed on additional advances and a bursary default.

The operating account receivable of \$77,512 at 31 March 1995 related to certain employee travel and payroll advances, Doctors' CMPA fees and nursing student stipends. Of the \$77,512, \$22,988 (which includes \$15,436 for a former executive employee) is in dispute by current and former employees who are arguing that the amounts were repaid. The Corporation is unable to confirm or deny this claim because of poor record keeping during the period the monies were advanced.



### 3.27 The Western Health Care Corporation

Figure 3

#### Western Health Care Corporation Patient Receivables 31 March

| Site                                         | 1999         |            |            | 1995         |            |              |
|----------------------------------------------|--------------|------------|------------|--------------|------------|--------------|
|                                              | Receivable   | Allowance  | Net        | Receivable   | Allowance  | Net          |
| Western Memorial Regional Hospital           | \$ 479,561   | \$ 103,979 | \$ 375,582 | \$ 902,728   | \$ 353,977 | \$ 638,751   |
| Bonne Bay                                    | 19,427       | 15,199     | 4,228      | 22,341       | 153        | 22,188       |
| Dr. J. I. O'Connell Centre                   | 391,043      | 346,308    | 44,735     | 166,024      | 74,697     | 91,327       |
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| Bay St. George Senior Citizen's Home         | 11,557       | 0          | 11,557     | 15,509       | Note 1     | 15,509       |
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### 3.27 The Western Health Care Corporation

- As at 31 March 1999, the Corporation was owed \$100,563 for travel advances and \$802,523 for payroll adjustments resulting from the consolidation of various payrolls of the former entities. Our review indicated the following:
  - Controls over the travel advances are inadequate as \$74,101 of the \$100,563 is considered uncollectible.
  - The payroll adjustments of \$802,523 are to be repaid by the employees when they terminate; however, this is not being done in all cases as there is \$25,130 owing from former employees.

### 3. Financial Operating Results

At the time of our review, the Corporation's financial operating results had deteriorated significantly. As separate entities, these facilities had a combined expenditure of approximately \$82 million for the year ended 31 March 1995 and \$88 million during the first year of consolidation in 1995-96. Expenditures for the next three fiscal years continued to increase as disclosed in Figure 4.

Figure 4

#### Western Health Care Corporation Financial Results Years Ended 31 March (\$ Millions)

|                                                  | 1995     | 1996     | 1997     | 1998     | 1999     | 2000    |
|--------------------------------------------------|----------|----------|----------|----------|----------|---------|
|                                                  | Actual   | Actual   | Actual   | Actual   | Actual   | Budget  |
| <b>Revenue</b>                                   |          |          |          |          |          |         |
| Provincial Plan                                  | \$ 69.2  | \$ 71.4  | \$ 73.6  | \$ 79.0  | \$ 76.7  | \$ 80.7 |
| Provincial Plan - one time payment               | -        | -        | -        | -        | 5.5      | -       |
| Other                                            | 12.9     | 14.9     | 16.5     | 16.9     | 17.0     | 21.8    |
| Total revenue                                    | 82.1     | 86.3     | 90.1     | 95.9     | 99.2     | 102.5   |
| <b>Expenditure</b>                               |          |          |          |          |          |         |
| Administrative and support services              | 28.4     | 34.1     | 34.1     | 35.9     | 35.1     | 39.8    |
| Nursing services                                 | 30.2     | 30.8     | 43.9     | 46.4     | 43.8     | 55.1    |
| Ambulatory care services                         | 6.4      | 6.4      | 4.9      | 5.2      | 9.4      | 7.2     |
| Diagnostic and therapeutic services              | 9.6      | 11.2     | 8.9      | 9.3      | 9.8      | 11.2    |
| Educational services                             | 1.8      | 1.7      | 2.1      | 2.4      | 2.3      | 3.6     |
| General services                                 | 5.7      | 2.9      | 0.9      | 0.9      | 1.5      | 1.0     |
| Community support program                        | 0.2      | 0.8      | 0.1      | 0.2      | 0.4      | 0.3     |
| Total expenditure                                | 82.3     | 87.9     | 94.9     | 100.3    | 102.3    | 118.2   |
| Operating deficit before other items             | (0.2)    | (1.6)    | (4.8)    | (4.4)    | (3.1)    | (15.7)  |
| <b>Other items</b>                               |          |          |          |          |          |         |
| Increase in severance and vacation pay accrual   | 0.5      | 0.7      | 0.6      | 1.7      | 1.1      |         |
| Amortization of capital assets                   | 1.1      | 1.2      | 2.0      | 2.4      | 2.8      |         |
| Amortization of deferred contributions - capital | -        | -        | (1.5)    | (1.5)    | (2.0)    |         |
| Special funding for prior years' deficits        | -        | -        | -        | -        | (8.7)    |         |
| Provincial plan revenue - mortgage repayments    | -        | -        | (0.1)    | -        | (0.1)    |         |
| Total other items                                | 1.6      | 1.9      | 1.0      | 2.6      | (6.9)    |         |
| <b>Excess of expenditure over revenue</b>        | \$ (1.8) | \$ (3.5) | \$ (5.8) | \$ (7.0) | \$ (3.8) |         |

Source: Audited financial statements and 1999-00 Budget.

### 3.27 The Western Health Care Corporation

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At the time of our review, the Corporation's financial operating results had deteriorated significantly. As separate entities, these facilities had a combined expenditure of approximately \$82 million for the year ended 31 March 1995 and \$88 million during the first year of consolidation in 1995-96. Expenditures for the next three fiscal years continued to increase as disclosed in Figure 4.

Figure 4

#### Western Health Care Corporation Financial Results Years Ended 31 March (\$ Millions)

|                                                  | 1995            | 1996            | 1997            | 1998            | 1999            | 2000          |
|--------------------------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|---------------|
|                                                  | Actual          | Actual          | Actual          | Actual          | Actual          | Budget        |
| <b>Revenue</b>                                   |                 |                 |                 |                 |                 |               |
| Provincial Plan                                  | \$ 69.2         | \$ 71.4         | \$ 73.6         | \$ 79.0         | \$ 76.7         | \$ 80.7       |
| Provincial Plan - one time payment               | -               | -               | -               | -               | 5.5             | -             |
| Other                                            | 12.9            | 14.9            | 16.5            | 16.9            | 17.0            | 21.8          |
| <b>Total revenue</b>                             | <b>82.1</b>     | <b>86.3</b>     | <b>90.1</b>     | <b>95.9</b>     | <b>99.2</b>     | <b>102.5</b>  |
| <b>Expenditure</b>                               |                 |                 |                 |                 |                 |               |
| Administrative and support services              | 28.4            | 34.1            | 34.1            | 35.9            | 35.1            | 39.8          |
| Nursing services                                 | 30.2            | 30.8            | 43.9            | 46.4            | 43.8            | 55.1          |
| Ambulatory care services                         | 6.4             | 6.4             | 4.9             | 5.2             | 9.4             | 7.2           |
| Diagnostic and therapeutic services              | 9.6             | 11.2            | 8.9             | 9.3             | 9.8             | 11.2          |
| Educational services                             | 1.8             | 1.7             | 2.1             | 2.4             | 2.3             | 3.6           |
| General services                                 | 5.7             | 2.9             | 0.9             | 0.9             | 1.5             | 1.0           |
| Community support program                        | 0.2             | 0.8             | 0.1             | 0.2             | 0.4             | 0.3           |
| <b>Total expenditure</b>                         | <b>82.3</b>     | <b>87.9</b>     | <b>94.9</b>     | <b>100.3</b>    | <b>102.3</b>    | <b>118.2</b>  |
| <b>Operating deficit before other items</b>      | <b>(0.2)</b>    | <b>(1.6)</b>    | <b>(4.8)</b>    | <b>(4.4)</b>    | <b>(3.1)</b>    | <b>(15.7)</b> |
| <b>Other items</b>                               |                 |                 |                 |                 |                 |               |
| Increase in severance and vacation pay accrual   | 0.5             | 0.7             | 0.6             | 1.7             | 1.1             |               |
| Amortization of capital assets                   | 1.1             | 1.2             | 2.0             | 2.4             | 2.8             |               |
| Amortization of deferred contributions - capital | -               | -               | (1.5)           | (1.5)           | (2.0)           |               |
| Special funding for prior years' deficits        | -               | -               | -               | -               | (8.7)           |               |
| Provincial plan revenue - mortgage repayments    | -               | -               | (0.1)           | -               | (0.1)           |               |
| <b>Total other items</b>                         | <b>1.6</b>      | <b>1.9</b>      | <b>1.0</b>      | <b>2.6</b>      | <b>(6.9)</b>    |               |
| <b>Excess of expenditure over revenue</b>        | <b>\$ (1.8)</b> | <b>\$ (3.5)</b> | <b>\$ (5.8)</b> | <b>\$ (7.0)</b> | <b>\$ (3.8)</b> |               |

Source: Audited financial statements and 1999-00 Budget.



### 3.27 The Western Health Care Corporation

A deficit of \$8.2 million was projected for 1998-99. However, the Department of Health advised the Corporation not to take any action, even though the Board had developed certain cost cutting measures to address the \$8.2 million projected deficit. The Corporation requested a response to these cost-saving measures on two occasions during the year; however, they did not receive any reply from the Department until April 1999, after the fiscal year, when additional funding of \$5.5 million was approved to help fund the 1998-99 deficit.

In total, the Department of Health and Community Services approved \$20.9 million in March 1999 to fund the following:

- \$8.7 million for accumulated operating deficits to 31 March 1998;
  - \$1.9 million for accumulated capital deficits to 31 March 1998;
  - \$4.8 million for a cash injection relating to capital items; and
  - \$5.5 million towards the operating deficit for 1998-99.
- \$20.9 million in additional funding**

Even with the additional \$5.5 million funding for 1998-99, and a reduction in expenditures compared to their budget, the Corporation still incurred a deficit of \$3.1 million. At the time of our review, the \$5.5 million was considered a one time grant and therefore may not be included as part of the 1999-2000 government funding. As a result, without significant cost reductions, the Corporation will again start to accumulate significant deficits.

The board has made improvements in the monitoring of its financial operations. Detailed monthly variance reports are prepared and distributed to individuals responsible for the expenditures, there are periodic variance explanations sought and year end reporting is more timely. The audit for the fiscal year ended 31 March 1999 was completed on 18 June 1999 and is a significant improvement from the previous year when the audit was not completed until 25 September 1998. Previous to 1998, the audited financial statements for 31 March 1996 and 1997 were not available until 16 months and 12 months after year end, respectively.

While there are improvements, the current financial reporting system does not address the differing levels of information required by various groups within the organization, such as the Board of Directors, the Executive and Department heads. As indicated above, the system only produces a very detailed report by site, by department and expense code. It does not produce a summary level report for the Executive and the Board. In order to produce such summary reports, the information must be manually entered into spreadsheets and summarized. This is a similar process for the budget preparation as the information is prepared using spreadsheets and then entered into the financial system.



### 3.27 The Western Health Care Corporation

#### Protection of Assets

Policies and procedures for monitoring and controlling financial resources, inventories and capital assets have been established; however, the compliance with these policies in certain areas is deficient.

##### 1. Inventories

In order to operate efficiently and effectively the Corporation must purchase supplies prior to their usage. As a result there is a need to implement physical and accounting controls over these assets to ensure they are adequately safeguarded. As at 31 March 1999 these inventories were valued at \$2.3 million and consisted of various groups as disclosed in Figure 5.

Figure 5

#### Western Health Care Corporation Inventories 31 March

|                      | Western Memorial<br>Regional Hospital | Other<br>Sites | Total<br>1999 | Total<br>1998 |
|----------------------|---------------------------------------|----------------|---------------|---------------|
| Plant Maintenance    | \$ 240,785                            | \$ -           | \$ 240,785    | \$ 248,683    |
| Food                 | 48,946                                | 52,076         | 101,022       | 101,666       |
| Materials & Supplies | 121,064                               | 76,941         | 198,005       | 71,059        |
| Drugs                | 415,076                               | 192,928        | 608,004       | 568,474       |
| Laboratory           | 155,448                               | -              | 155,448       | 142,578       |
| Orthopaedic          | 115,933                               | -              | 115,933       | 97,617        |
| Main Stores          | 548,890                               | 301,827        | 850,717       | 827,444       |
| Other-Fuel           | -                                     | 12,216         | 12,216        | 20,032        |
| Total                | \$ 1,646,142                          | \$ 635,988     | \$ 2,282,130  | \$ 2,077,553  |

Source: Western Health Care Corporation financial records:

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#### Protection of Assets

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| Other-Fuel           | -                                     | 12,216         | 12,216        | 20,032        |
| Total                | \$ 1,646,142                          | \$ 635,988     | \$ 2,282,130  | \$ 2,077,553  |

Source: Western Health Care Corporation financial records:

### **3.27 The Western Health Care Corporation**

As Western Memorial Regional Hospital represented 72% of the inventories, our review included an examination of controls over these inventories. This review identified the following:

- Inventory procedures require physical counts every three months for the main stores inventory; however, as of 21 July 1999, no count had been performed as scheduled for the three month period ending 30 June 1999. Only one count had been performed after September 1998, this being the 31 March 1999 count for year end auditing purposes.
- Medical and surgical supplies, until requisitioned to various departments, are stored in the main stores area along with other inventories. These supplies are accessible by anyone making deliveries to the receiving area. In addition, medical and surgical supplies requisitioned by various hospital departments are stored in a Clean Holding Room on each floor. This room is supposed to be locked with access limited to stock handlers and nursing staff; however, on a number of visits to one area during the audit, the room was unlocked and unsupervised.
- Perpetual inventory record keeping systems are not maintained for all inventories. Only the main stores inventory located at the Western Memorial Regional Hospital, the Sir Thomas Roddick Hospital and the Charles L. LeGrow Hospital and the pharmacy inventory at the Western Memorial Regional Hospital were controlled by perpetual records. Inventories were counted as at 31 March 1999 and perpetual records were adjusted for any variances. Our review of these variances indicated that they were not material in dollar amount; however, the number of variances were significant. The number of inventory items having variances ranged from 20% (340 of 1691 items) at the Charles L. LeGrow Hospital to 67% (1173 of 1735 items) at the pharmacy in the Western Memorial Regional Hospital. As a result we performed test counts of the Corporation's inventories and identified numerous discrepancies.
- Weaknesses were also identified in the year end accounting for inventories. For the year end 31 March 1998, a \$271,000 adjustment was required as a result of errors in the timing and recording of the receipt of goods. For the year end 31 March 1999, the Main Stores inventory located at the Sir Thomas Roddick Hospital was overstated by approximately \$19,000 due to adjusting the inventories prior to the investigation of variances.





### 3.27 The Western Health Care Corporation

#### 2. Capital Assets

As at 31 March 1999, the Corporation reported \$53.2 million in capital assets as recorded in Figure 6.

Figure 6

**Western Health Care Corporation**  
**Capital Assets**  
**31 March**  
**(\$ Millions)**

|                       | Cost    | Accumulated<br>Depreciation | Total<br>1999 | Total<br>1998 |
|-----------------------|---------|-----------------------------|---------------|---------------|
| Land                  | \$ 0.3  | \$ -                        | \$ 0.3        | \$ 0.3        |
| Equipment under lease | 0.6     | 0.2                         | 0.5           | 0.5           |
| Buildings             | 18.5    | 8.5                         | 10.0          | 10.4          |
| DVA unit              | 3.6     | 0.4                         | 3.2           | 3.4           |
| Parking lot           | 0.3     | 0.1                         | 0.2           | 0.2           |
| Equipment             | 29.7    | 19.5                        | 10.1          | 10.3          |
| Motor vehicles        | 0.2     | 0.2                         | -             | -             |
| Total                 | \$ 53.2 | \$ 28.9                     | \$ 24.3       | \$ 25.1       |

Source: Audited financial statements.

A review of the Corporation's controls over its capital assets identified the following concerns:

- Presently the Corporation does not have a complete capital asset ledger; however, a capital asset listing has been started for all new assets purchased since December 1998. Also, a computer listing has been completed for all computers excluding laser printers. This listing indicates asset number, location, description and usage of each computer; however, it does not record the serial number. The listings, however, do not provide cost information and as a result a reconciliation of these physical records to accounting records cannot be performed.

### 3.27 The Western Health Care Corporation

#### 2. Capital Assets

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Figure 6

**Western Health Care Corporation**  
**Capital Assets**  
**31 March**  
**(\$ Millions)**

|                       | Cost    | Accumulated<br>Depreciation | Total<br>1999 | Total<br>1998 |
|-----------------------|---------|-----------------------------|---------------|---------------|
| Land                  | \$ 0.3  | \$ -                        | \$ 0.3        | \$ 0.3        |
| Equipment under lease | 0.6     | 0.2                         | 0.5           | 0.5           |
| Buildings             | 18.5    | 8.5                         | 10.0          | 10.4          |
| DVA unit              | 3.6     | 0.4                         | 3.2           | 3.4           |
| Parking lot           | 0.3     | 0.1                         | 0.2           | 0.2           |
| Equipment             | 29.7    | 19.5                        | 10.1          | 10.3          |
| Motor vehicles        | 0.2     | 0.2                         | -             | -             |
| Total                 | \$ 53.2 | \$ 28.9                     | \$ 24.3       | \$ 25.1       |

Source: Audited financial statements.

A review of the Corporation's controls over its capital assets identified the following concerns:

- Presently the Corporation does not have a complete capital asset ledger; however, a capital asset listing has been started for all new assets purchased since December 1998. Also, a computer listing has been completed for all computers excluding laser printers. This listing indicates asset number, location, description and usage of each computer; however, it does not record the serial number. The listings, however, do not provide cost information and as a result a reconciliation of these physical records to accounting records cannot be performed.

### 3.27 The Western Health Care Corporation

- As a result of the significant risk to the Corporation if equipment should fail to operate properly, it is necessary to maintain a record of each significant piece of equipment and the repairs and maintenance relating to that equipment to ensure that all equipment is properly maintained and that information required for equipment replacement is readily available. The Corporation does have a computerized system to track scheduled and unscheduled maintenance; however, our review identified the following:
  - The system is not kept up to date as maintenance performed is not always entered into the system. For example, the preventative maintenance completed on X-Ray equipment in February 1999 was not entered into the computer as of July 1999.
  - We were informed that preventative maintenance is not always performed as scheduled due to a lack of staff. In addition, our review indicated that the computerized system used to track maintenance is not accurate. Out of a sample of 15 pieces of biomedical equipment selected from the computerized system, the system indicated that no preventative maintenance was completed during the last two years on these 15 pieces although scheduled. Our review of files relating to these 15 pieces of equipment indicated that one piece of equipment had in fact had recent maintenance.
  - Although the computerized system can provide a listing of equipment requiring maintenance, this feature is not used to schedule required maintenance.
  - The Corporation has not established any policies to address the maintenance of biomedical and other equipment.
  - The system is not Y2K compliant.

Another important aspect of equipment maintenance is to maintain a record of external maintenance contracts to ensure that they are kept current and all equipment is maintained in accordance with the contract. The Corporation presently relies on an informal system to track these contracts which consists of a dependency on vendors to advise them as to when contracts are to be renewed and the use of a manual maintenance contract file. However, upon review of the maintenance contract file only two of the six items

### 3.27 The Western Health Care Corporation

included were current contracts. After some search, five more contracts were located at different sites and departments.

We also note that a log book is kept on a CAT Scan which records regular monthly preventative and non-scheduled maintenance completed partially by the vendor and partially by the staff. There is also some mobile medical equipment that have tags stating their last maintenance date by the maintenance vendor.

- Monitoring of cellular phones is inadequate. For the past two years the 26 cellular phones have cost more than \$19,000 annually. Most of the cost is associated with the usage of the phones while out of the province on business. For one bill ending 14 February 1999, the roamer usage averaged \$51 per day for 12 days. The evaluation of the rental packages should be carried out on a regular basis to match each user with the most cost effective usage package.
- The Corporation has 27 vehicles. The Corporation does not monitor the operating costs of each vehicle. Log books are used to schedule vehicle usage; however, they are not used to track the mileage of each vehicle to ensure they are always used as scheduled. While the Corporation has policies in place to monitor the maintenance of vehicles, the scheduling of maintenance is not recorded on a timely basis in the computerized system.
- The Corporation owns 44 properties throughout the region which are mainly used for doctors, interns, student and other staff residences. Currently there is no system in place to adequately monitor the cost of each property as not all properties have separate cost centres in the general ledger. Out of the 44 properties, 34 are furnished; however, the Corporation does not maintain furniture listings for these properties. A proposal for more efficient means of control is in the final approval stages including setting up cost centres for each property and tracking all moveable assets.

In 1998-99 two of the Corporation's housing properties were sold, one for a profit of \$23,000 and the other at a loss of \$32,000. The property sold at a loss was purchased for \$62,000 in 1993 and sold for \$32,600 in 1998. Staff indicated this property was in need of repairs.

### 3.27 The Western Health Care Corporation

#### Purchasing

During the fiscal year 1998-99, the Corporation spent approximately \$24.9 million on goods and services including capital purchases. The Corporation's Materials Management Department is responsible for the purchasing of goods and services. Policies and procedures have been established and communicated to staff through a policy and procedures manual which covers such areas as general purchasing, public tenders and hiring external contractors.

#### 1. Public Tender Act

Policies and procedures have been established to ensure that supplies are being acquired economically and efficiently. These include the requirement that three quotes be obtained for purchases under \$7,500 and public tenders be issued for goods and services with a value greater than \$7,500 (\$10,000 after June 1998) as required by the *Public Tender Act*.

Our review of the Materials Management Department for compliance with these policies and government requirements disclosed that, for goods and services purchased below the public tender thresholds, the Materials Management Department maintains a record of quotes and a review of a sample of 10 purchases under \$10,000 disclosed that the purchases were made in compliance with the *Public Tender Act*.

We reviewed a total of 25 purchases to determine whether the Corporation was complying with the *Public Tender Act*. We selected 4 purchases from 1996-97 for goods and services exceeding \$5,000, 10 purchases from 1997-98 for goods and services exceeding \$7,500, and 11 purchases from 1998-99 for goods and services exceeding \$10,000. Our review indicated the following:

- 15 purchases, made through public tenders, were in compliance with the *Public Tender Act*;
- 4 purchases were made through external agencies, the Department of Health and Community Services, the Department of Works, Services and Transportation, the Newfoundland and Labrador Health and Community Services Association and an external consultant, and complied with the *Public Tender Act*;
- 3 purchases were not tendered, the required Form B was completed, and the purchases were reported to the House of Assembly as required by the *Public Tender Act*. The Corporation indicated that these purchases were acquired from the only available source and related to equipment maintenance from the original vendor.



### 3.27 The Western Health Care Corporation

- 2 purchases were not tendered and the Form B was not completed and as a result did not comply with the *Public Tender Act*. These purchases were as follows:

| Invoice #  | Date       | Description                       | Amount   |
|------------|------------|-----------------------------------|----------|
| 5631       | Aug. 1997  | Software Service Contract         | \$49,045 |
| C100003561 | Sept. 1997 | Professional Development Supplies | \$70,122 |

- 1 purchase was awarded to the preferred bidder as a result of a tender call. However, after awarding the tender to the preferred bidder, the Corporation had to cancel the tender after it realized that it already had a contract with an existing supplier that could not be terminated without proper notice. The preferred bidder was paid \$50,000 by the Corporation as an out of court settlement.

#### 2. Travel

Our previous review in 1996 identified significant weaknesses over travel expenses particularly with the use of corporate credit cards. At that time, the Corporation would pay employee corporate credit card bills and recover any personal expenses from the employee. The amount recovered depended on the employee identifying the purchase as a personal item. In addition, amounts claimed as travel expenditures were not always supported by receipts.

Travel costs for the past two years are disclosed in Figure 7. As the figure shows, travel costs exceeded budgeted travel costs for 1998-99 by \$61,414.

Since our last review, the Corporation has implemented a policy whereby it no longer pays corporate credit card balances except for one card used for patient escort travel. Our current review did not identify any unrecovered personal expenses paid by the Corporation; however, we did identify some minor payments which were not properly supported by receipts. We were informed that, in future, all payments will be properly supported.



### 3.27 The Western Health Care Corporation

Figure 7

**Western Health Care Corporation  
Travel Costs  
31 March**

| <b>Travel<br/>Description</b> | <b>Actual<br/>1998</b> | <b>Actual<br/>1999</b> | <b>Budget<br/>1999</b> |
|-------------------------------|------------------------|------------------------|------------------------|
| Escort                        | \$ 55,426              | \$ 68,919              | \$ 66,700              |
| Education/Convention          | 141,708                | 167,429                | 190,500                |
| Regional/Local                | 441,360                | 441,033                | 423,446                |
| Locums                        | 248,573                | 207,152                | 226,400                |
| Medical Staff                 | 104,266                | 125,999                | 123,350                |
| Recruitment and relocation    | 360,742                | 346,821                | 267,200                |
| Other                         | 827                    | 1,857                  | 200                    |
| <b>Total Travel</b>           | <b>\$ 1,352,902</b>    | <b>\$ 1,359,210</b>    | <b>\$ 1,297,796</b>    |

Source: Western Health Care Corporation financial records.

### 3. Employee Benefits

Employee benefits in excess of government policy noted during our previous review have been eliminated or reduced. Voluntary group insurance premiums and dental insurance premiums are now paid 100% by employees, similar to other public sector employees. However, long term disability premiums are cost shared with the applicable employees on a 50/50 basis compared to other public sector employees who are required to pay 100% of the premiums. This cost the Corporation \$10,627 in 1998-99.

The Corporation now issues certificate and service pins for reaching certain levels of service. Gifts of watches are now given on retirement or at the discretion of the Chief Executive Officer. The Corporation still contributes to employee Christmas parties; however, the contribution is limited to \$3 per employee.



### 3.27 The Western Health Care Corporation

Figure 7

**Western Health Care Corporation**  
**Travel Costs**  
**31 March**

| <b>Travel Description</b>  | <b>Actual 1998</b>  | <b>Actual 1999</b>  | <b>Budget 1999</b>  |
|----------------------------|---------------------|---------------------|---------------------|
| Escort                     | \$ 55,426           | \$ 68,919           | \$ 66,700           |
| Education/Convention       | 141,708             | 167,429             | 190,500             |
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### 3.27 The Western Health Care Corporation

In 1997, a former executive of the Corporation was paid severance pay of \$40,589 for the maximum 20 years of service. However, this employee did not retire but accepted another position with the Corporation. The severance benefits were not repaid and the employee is still accruing service with the Corporation which included the 20 years that were already paid. This will result in a duplicate payment of severance on retirement of the employee. Government requires the repayment of severance in accordance with a prescribed formula when an employee is rehired within Government.

In 1998, another former executive terminated employment with the Corporation and received a payment of \$30,000. This did not represent severance as the employee accepted employment with another public service entity and, in accordance with Government policy, carried the years of service forward to that entity. There was no authority for the Corporation to pay this \$30,000.

Government policy does not permit the provision of monetary and non-monetary benefits in excess of approved scales. Minute of Council 94-0520, dated 2 June 1994, directed Treasury Board to advise all boards *"...that compliance in all aspects with the compensation standards which have been established for Government departments is mandatory."* Currently the Corporation is paying a senior official more than the highest step on the executive pay plan in addition to an annual bonus of \$5,000. This employee is receiving a car allowance of \$750 per month which is in excess of the \$85 car allowance provided by government. The Corporation has also agreed to reimburse this employee 24 months of salary in lieu of notice of termination of the employment contract even though government's maximum payment is 62 weeks. The Department of Health and Community Services is aware of these payments and Cabinet has approved this contract.

#### Human Resources

For the year ended 31 March 1999 \$79.3 million or 76% of total shareable expenses represented salary related costs. A significant impact on these costs has been the amount of sick leave and the resulting replacement cost. Since our review in 1996 sick leave costs have increased 15% for the entities under the former Western Memorial Hospital while the other entities also have high sick leave costs as disclosed in Figure 8.

As indicated in Figure 8, it cost the Corporation \$2.5 million to replace employees who were on sick leave in 1998-99.

### 3.27 The Western Health Care Corporation

Figure 8

#### Western Health Care Corporation Sick Leave 31 March

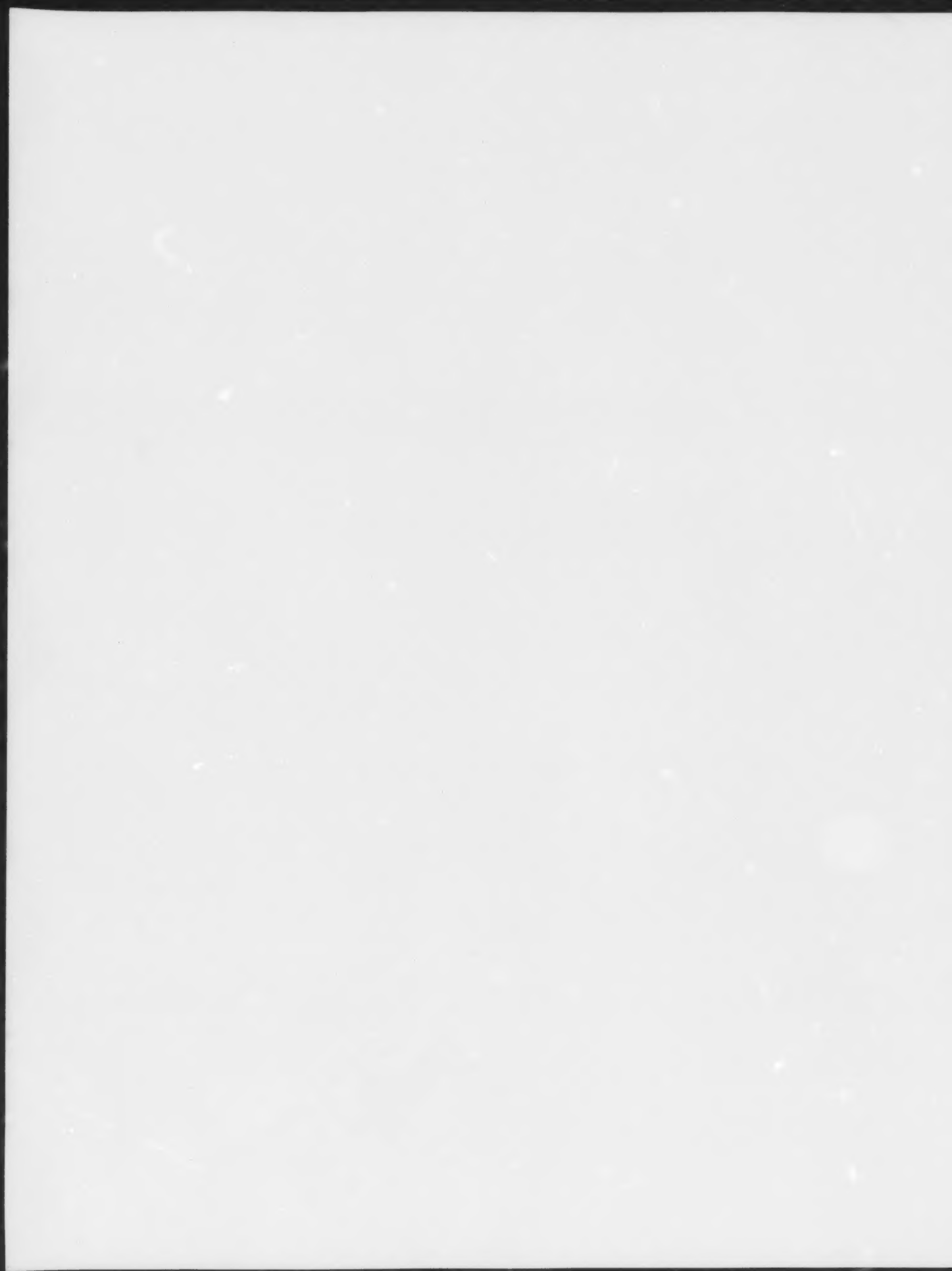
| Site                                 | 1999                                    |                  |                            |                  |              | 1995                       |                               |
|--------------------------------------|-----------------------------------------|------------------|----------------------------|------------------|--------------|----------------------------|-------------------------------|
|                                      | Budgeted Full-time Equivalent Positions | Total Sick Hours | Average hours per employee | Replacement Cost |              | Average hours per employee | Replacement Cost Per Employee |
|                                      |                                         |                  |                            | Total (000's)    | Per Employee |                            |                               |
| Western Memorial Regional Hospital   | 794                                     | 121,971          | 154                        | \$ 1,250         | 1,574        | 131                        | \$ 1,172                      |
| Bonne Bay                            | 44                                      | 9,482            | 216                        | 101              | 2,295        | 118                        | 1,192                         |
| Dr. J. I. O'Connell Centre           | 133                                     | 20,420           | 154                        | 274              | 2,061        | 145                        | 1,820                         |
| Calder Health Centre                 | 44                                      | 6,373            | 145                        | 72               | 1,636        | 82                         | 658                           |
|                                      | 1,015                                   | 158,246          | 156                        | 1,697            | 1,672        | 129                        | 1,227                         |
| Interfaith Home for Senior Citizens  | 84                                      | 13,707           | 163                        | 159              | 1,896        |                            |                               |
| Medical staff                        | 61                                      | 1,064            | 17                         |                  | 8            |                            |                               |
| Rufus Guinchard Health Centre        | 45                                      | 5,852            | 130                        | 59               | 1,311        |                            |                               |
| Bay St. George Senior Citizen's Home | 131                                     | 26,302           | 201                        | 271              | 2,069        |                            |                               |
| Sir Thomas Roddick Hospital          | 179                                     | 26,107           | 146                        | 238              | 1,330        |                            |                               |
| Dr. Charles L. Legrow Health Centre  | 90                                      | 8,695            | 97                         | 89               | 991          |                            |                               |
| Relief Staff                         | 293                                     | -                | -                          | -                | -            |                            |                               |
|                                      | 1,898                                   | 239,973          | 126                        | 2,513            | 1,324        |                            |                               |

Source: Western Health Care Corporation human resources reports.

#### Recommendations

##### *The Corporation should:*

- *continue to closely monitor its financial position and, in consultation with the Department of Health and Community Services, take action to address the annual deficits;*
- *address the deficiencies in controls over capital assets and inventories as these represent a significant investment of public funds;*
- *comply with Government and Board Policy in such areas as public tendering, travel and employee benefits; and*
- *take steps to address the high costs of staff sick leave.*





### 3.27 The Western Health Care Corporation

Figure 8

#### Western Health Care Corporation Sick Leave 31 March

| Site                                 | 1999                                    |                  |                            |                  |              | 1995                       |                               |
|--------------------------------------|-----------------------------------------|------------------|----------------------------|------------------|--------------|----------------------------|-------------------------------|
|                                      | Budgeted Full-time Equivalent Positions | Total Sick Hours | Average hours per employee | Replacement Cost |              | Average hours per employee | Replacement Cost Per Employee |
|                                      |                                         |                  |                            | Total (000's)    | Per Employee |                            |                               |
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| Dr. J. I. O'Connell Centre           | 133                                     | 20,420           | 154                        | 274              | 2,061        | 145                        | 1,820                         |
| Calder Health Centre                 | 44                                      | 6,373            | 145                        | 72               | 1,636        | 82                         | 658                           |
|                                      | 1,015                                   | 158,246          | 156                        | 1,697            | 1,672        | 129                        | 1,227                         |
| Interfaith Home for Senior Citizens  | 84                                      | 13,707           | 163                        | 159              | 1,896        |                            |                               |
| Medical staff                        | 61                                      | 1,064            | 17                         |                  | 0            |                            |                               |
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- *comply with Government and Board Policy in such areas as public tendering, travel and employee benefits; and*
- *take steps to address the high costs of staff sick leave.*

## **3.27 The Western Health Care Corporation**

### **Corporation's Response**

#### ***Financial Management***

##### ***1. Financial Position***

*The Corporation has financed its operations through Line of Credit and Bankers Acceptance resulting in significant interest charges. In accordance with government policy these interest costs must be charged to the Board of Trustees Fund rather than to the Operating Fund. The Corporation has requested that these interest charges be considered shareable expenses, and charged to the Operating Fund, as they are a direct result of ensuring adequate cash flow to operating its facilities. The Corporation has previously addressed this with the Department of Health and Community Services.*

*Eighty percent (80%) of our accumulated operating deficit as at March 31, 1999 relates to vacation and severance pay accruals. The Provincial Government will fund these amounts when paid by the Corporation and our accumulated deficit reduced accordingly. With this element removed, our recent history indicates a decline in our operating deficit from year to year (\$4.7 million - 1997; \$4.4 million - 1998; \$3.0 million - 1999).*

*The Corporation is projecting a \$15.7 million deficit for fiscal 2000. This deficit is forecasted if the present level of service is to be maintained without additional funding from Government.*

*The \$700,000 capital deficit noted in the report is a result of prior years operations rather than the fiscal 1999 year. This deficit is a result of the accounting treatment applied to capital purchases. Funding received for capital purchases is recorded on the balance sheet as deferred capital and amortized over the life of the asset purchased in the same manner as the asset costs are amortized. When assets are purchased without funding, the amount of deferred capital amortized is less than the asset costs amortized. Consequently, the annual amortization of the capital costs is greater than the amortization of deferred capital contributions resulting in a capital deficit for the year. If the equipment had been purchased with monies funded, these two annual amortization amounts would offset each other. The Corporation no longer purchases capital assets without funding.*

##### ***2. Accounts Receivable***

*The Corporation's accounts receivable position has improved in the last year. The Corporation has taken a conservative approach in relation to its allowance for doubtful accounts for all account receivable balances. Much of the receivable balances relate to past years for which information is minimal. Consequently, it is extremely difficult to conduct the proper*

### 3.27 The Western Health Care Corporation

*follow up and collection on the accounts. Collection activities are ongoing and we are meeting with success in collections. The Corporation feels that it is prudent at this time to take a conservative stance with regard to the allowance for doubtful accounts. Current accounts receivable processes are up to date. Consequently, our position has not worsened in the last year.*

*The comment regarding the requirement for the Board of Trustees Fund to assume responsibility for the interest charges related to operating deficits is an issue for our Corporation. We have requested that these interest charges be considered a shareable expense since the sole purpose for its existence is to allow for adequate cash flows to operate the health care institutions. We have addressed this with the Department of Health and Community Services in the past and have requested that this policy be reviewed and changed to allow this expense to be considered shareable and funded by Provincial Plan Revenue.*

*As noted previously, the majority of our patient receivable balance is carried forward from previous years. We have allowed for 51% of our March 31, 1999 patient receivable balance, as the majority of this allowance is made up of 13 long term care patient balances. If these balances are excluded from the calculation, a normalized allowance percentage is made, ie. 30%. As stated previously, the Corporation has taken a conservative approach on the old balances.*

*There are disputed amounts recorded in our records that have been fully provided for in our allowance for doubtful accounts. In light of the lack of documentation the Corporation felt it prudent to provide for the full amount of the receivable balances at this time. Any future collections will result in an adjustment to the allowance.*

*Collection activities are ongoing on all prior years' balances. In the past months we have implemented new procedures surrounding travel advances and the impact appears favorable. Additionally, the Corporation has targeted the travel advance area for full review in the coming year. All processes surrounding travel advances will be studied to develop recommendations to increase control, reduce risk and ensure collectibility.*

*The payroll adjustments noted stem from a policy change in 1992. Some employees have left the organization without repaying amounts owed, however, these employees terminated prior to 1996. Controls and processes are now in place to safeguard against this happening in the future.*

## **3.27 The Western Health Care Corporation**

### **3. Financial Operating Results**

*The Corporation's operating expenses have increased over the past four years. This is primarily due to increases in salaries, drug costs, additional staff required to serve our aging population and increasing patient acuity. Over this same time frame Provincial funding has also increased. Our operating deficit has decreased over the past three years (\$4.7 million - 1997; \$4.4 million - 1998; \$3.0 million - 1999). These deficits will continue, however, if we are to maintain our current level of service without increases in funding.*

*The Corporation has recognized the fact that it was unable to provide adequate reports for all levels of management. Consequently, we are in the process of implementing the Meditech Information System that will address the reporting issues raised. This system will be able to provide a variety of reports tailored to the needs of the user dependant upon their position in the Corporation. To date we have already witnessed improvements in the information provided. When this system is fully implemented, greater benefits will be realized.*

### **Protection of Assets**

#### **1. Inventories**

*The Corporation has implemented tighter controls over inventory. A full inventory count was conducted on July 31, 1999 immediately prior to moving to the Meditech Information System. Another cycle count is planned for November 30, 1999. In addition to these formal counts, Materials Management staff perform spot checks on historically problematic items on a daily basis. These daily spot checks will be fully documented in the future. Materials Management staff have been directed to pay special attention in future counts. These errors should not recur.*

*With regards to the accessibility of medical and surgical supplies in the central stores department, options are being investigated to remove or mitigate this exposure. Access to supplies on nursing floors will also be evaluated and corrective action taken as required ensuring adequate security of corporate assets.*

#### **2. Capital Assets**

*The Corporation is in the process of requesting proposals from vendors to supply a fixed asset and asset maintenance management system. This system will track all asset additions and disposals as well as produce all fixed asset costing and depreciation schedules. When this system is selected and implemented, a complete inventory of capital assets will be*

### **3.27 The Western Health Care Corporation**

*undertaken to populate the system. Annual counts of capital assets will be conducted from that time forward.*

*The Corporation has a computerized Materials Management in place that is not Y2K compliant. This system will be replaced within the coming months. Your review found occurrences where a scheduled preventative maintenance was not entered into the system and occurrences where preventative maintenance was not completed as scheduled.*

*Workload demands we prioritize urgent and episodic Maintenance and in these cases accurate records are kept. With the installation of our new Materials Management System and with consultation with the recently established Equipment Services Regional Performance Improvement Team we will refine the department and its efficient functioning.*

*The Corporation has established a performance improvement team specifically related to equipment maintenance. This team will be establishing maintenance policies for all equipment for the Corporation.*

*Past filing of external maintenance contracts was inadequate. Since your audit, we have centralized the filing for all equipment maintenance contracts within the Equipment Maintenance Department.*

*A review of the cellular phone packages used by the Corporation will be reviewed on a continual basis to ensure the most cost-effective package is used for each user.*

*Separate responsibility centers have been established for all rental properties owned by the Corporation. This will assist management in monitoring the costs associated with these properties. All furniture and equipment in these facilities will be maintained in the new fixed asset system noted earlier. One staff member has also been assigned with the responsibility of monitoring the operations of these rental properties and ensuring that all appropriate revenues and expenses are charged to the particular rental property. Additionally, we have standardized the furnishings we provide in these properties.*

#### **Purchasing**

##### **1. Public Tender Act**

*The two purchases noted that failed to have the required Form B completed were oversights by our management staff. Each year we take measures to update staff on the requirements of the Public Tender Act. The management staff involved in these instances has had the requirements of the Act reviewed with them. Efforts will be made to continue to educate staff on the requirements.*



### **3.27 The Western Health Care Corporation**

#### **2. Travel**

*The most significant variance from budget for 1999 as outlined in your table is the Recruitment and Relocation Travel. These expenses are paid in accordance with government policy and increase with success in our recruitment efforts. It is difficult to accurately budget this expense given that we do not know from where we will be able to successfully recruit doctors and other staff.*

*It is policy that receipts accompany all travel/expense reports. All expense reports are scrutinized by managers prior being approved for payment. Managers are responsible for ensuring that all expenses claimed are reasonable and legitimate.*

#### **3. Employee Benefits**

*The Corporation attempted to discontinue the long-term disability program for managers. However, a number of managers with pre-existing medical conditions advised that they would not be able to obtain coverage elsewhere. The Corporation's legal council advised that to discontinue the program could leave the Corporation exposed to legal action from our managers. It was decided to return to the 50-50 arrangement to limit the Corporation's exposure. New managers are not eligible for this benefit.*

*The payment of severance pay to this former executive was a special situation. Severance has been paid, however, the employee is not eligible to receive this pay a second time when leaving the organization. A note has been made in the employee's file to this fact.*

*The payment made to this former executive was a payment in lieu of notice. This payment was based on a recommendation from legal counsel, to mitigate any recourse this former employee may have against the Corporation.*

*The senior official who is paid in excess of Step 33 on the Executive Pay Plan occupies a position that has not been formally classified through the classification process. The position identified fulfills two roles that are occupied and funded as two separate positions in other regional health boards.*

*The funding level provided was approved by government prior to the Corporation contracting.*



### **3.27 The Western Health Care Corporation**

#### ***Human Resources***

##### ***Sick Leave***

*Part of the reason for the increase in sick leave cost, as compared to 1996, is the increase in the cost of labour since that year.*

*During the past year we have held information sessions for all of our managers regarding the sick leave provisions of the various collective agreements. We have also reviewed all attendance records for employees throughout the region to attempt to identify issues that need to be addressed. Managers feel very restricted in their management of this problem by the wording which exists in the union agreements.*

### 3.28 Peninsulas Health Care Corporation

#### Introduction

The Peninsulas Health Care Corporation was established in January 1996 and operates under the authority of the *Hospitals Act*. Its operations are governed by a Board of Directors comprised of 18 members appointed by the Minister of Health and Community Services. The Corporation provides primary, secondary, ambulatory and long-term health care services to 58,000 people. It does this through two hospitals, three health care centres and two nursing homes covering a geographical region from Grand Bank to Bonavista, as portrayed by Figure 1.

**Figure 1**

#### Peninsulas Health Care Corporation Geographical Boundary 31 March 1999

| Location and Facility                             | Beds       |            |            | Population    | Map                                                                                  |
|---------------------------------------------------|------------|------------|------------|---------------|--------------------------------------------------------------------------------------|
|                                                   | Acute      | Long-term* | Total      |               |                                                                                      |
| Burin Peninsula Health Care Centre, Burin         | 54         |            | 54         | 17,000        |  |
| Dr. G.B. Cross Memorial Hospital, Clarenville     | 51         | 14         | 65         | 17,500        |                                                                                      |
| Bonavista Peninsula Health Centre, Bonavista      | 10         | 13         | 23         | 12,000        |                                                                                      |
| Golden Heights Manor, Bonavista                   |            | 60         | 60         |               |                                                                                      |
| Grand Bank Community Health Centre, Grand Bank ** | 4          |            | 4          | 7,000         |                                                                                      |
| Blue Crest Nursing Home, Grand Bank               |            | 71         | 71         |               |                                                                                      |
| U.S. Memorial Health Centre, St. Lawrence         |            | 30         | 30         | 4,500         |                                                                                      |
| <b>Total</b>                                      | <b>119</b> | <b>188</b> | <b>307</b> | <b>58,000</b> |                                                                                      |

\* Long-term beds include protective care

\*\* This represents holding beds

Source: Peninsulas Health Care Corporation

### **3.28 Peninsulas Health Care Corporation**

#### **Scope and Objectives**

We completed our review of the Peninsulas Health Care Corporation in January 1999. This review was directed primarily toward management practices, purchasing, and human resources and included testing for compliance with the various authorities under which the Corporation operates. This review was designed to assess whether:

- management practices were adequate to provide information to management and the Board for planning, decision making, control and ensuring compliance with legislative requirements;
- purchases, including capital assets and inventory, were adequately monitored, controlled, safeguarded and complied with Board policies and statutory requirements; and
- the human resource's function was adequate to provide for planning and control of human resources.

#### **Conclusions**

##### **Financial Position**

The Corporation has incurred deficits each fiscal year since it was established in 1996. The deficit, including non-shareable expenses, as reported in the Corporation's audited financial statements was \$700,000 in 1996-97, \$2.3 million in 1997-98 and \$2.0 million in 1998-99.

In 1997, Government approved a \$20 million health stabilization fund for 1997-98. This resulted in the Corporation receiving a one time payment of \$966,000 which was used to reduce the 1997-98 deficit to the reported \$2.3 million.

When Government approved the payment of \$966,000 from the health stabilization fund, it was expected to eliminate the Corporation's projected deficit of \$889,000 in 1997-98. However, the Corporation experienced difficulty in following its financial plan and as a result, it continued to incur a steadily increasing deficit for the 1997-98 fiscal year. As indicated above, the deficit for 1997-98 was \$2.3 million.

In 1998-99, Government provided an additional \$40 million to eliminate the accumulated deficits of the regional hospital boards as at 31 March 1998. The Corporation received \$3.9 million of this amount toward its accumulated deficit of \$8.4 million at 31 March 1998. The remaining accumulated deficit of \$4.5 million at 31 March 1998 relates to severance pay and annual leave accruals which Government will not fund.

Also, in 1998-99, an additional \$10 million was approved as one time funding to health care boards. The Corporation received \$1 million of this

### **3.28 Peninsulas Health Care Corporation**

amount; however, it still had an unfunded deficit of \$2.0 million for 1998-99 which increased the accumulated deficit of \$4.5 million to \$6.5 million.

#### **Capital Assets**

The Corporation has \$29.4 million in capital assets. These assets are not adequately controlled. The Corporation does not have a capital asset ledger to record each individual asset and related information. As well, not all assets are physically identified and periodic physical counts are not performed. Without this information, the Corporation does not know whether all of its capital assets are still on hand.

The Corporation does not have either a database of maintenance performed on capital equipment or a listing of maintenance contracts relating to each significant piece of capital equipment. As a result, records at the Corporation are not readily available to demonstrate that all significant pieces of equipment are properly maintained.

#### **Human Resources**

In the past two years the Corporation has undertaken a number of studies to address human resource issues such as sick leave, employee moral and communication problems. This is particularly significant since human resource costs represent 76% of the Corporation's expenditures.

The Corporation is having difficulty attracting and retaining salaried doctors. When the Corporation has to retain the services of locum doctors, there are extra costs. For the year ended 31 March 1998, the Corporation spent \$741,000 more than it budgeted for locum doctors and \$500,000 less than budget for salaried physicians. As a result the Corporation spent an additional \$241,000 providing the required service.

Sick leave, including replacement costs, cost the Corporation in excess of \$2 million in each of the past two years. This represented approximately 91,000 hours in 1997-98 (1996-97: 87,500 hours) or 116 hours (1996-97: 115 hours) per full-time position.

#### **Expenditures**

Inefficiencies in management information systems relating to the consolidation of the three predecessor hospital boards in 1996 continue to exist. The Board continues to operate two accounting systems, two inventory systems, two payroll systems and two leave systems. The Corporation is not realizing the economies of scale associated with having one headquarters office to provide all required administrative and accounting services.

### 3.28 Peninsulas Health Care Corporation

#### Findings and Recommendations

#### Management Practices

##### 1. Financial Results

Over the last three years the Corporation has been reporting a steadily weakening financial position. As at 31 March 1998 the Corporation had an accumulated deficit of \$8.4 million, a working capital deficit of \$5.3 million and a bank indebtedness of \$2.3 million. As at 31 March 1999, the bank indebtedness was \$4.6 million. Figure 2 shows the financial position of the Corporation for the years ended 31 March 1997, 1998, and 1999.

**Figure 2**

#### Peninsulas Health Care Corporation Financial Position For the Years Ended 31 March (\$ Millions)

| Description                           | 1997           | 1998           | 1999           |
|---------------------------------------|----------------|----------------|----------------|
| Receivables                           | \$ 1.7         | \$ 1.5         | \$ 9.4         |
| Inventory                             | 0.7            | 0.8            | 0.8            |
| Prepaid expenses                      | 0.1            | 0.2            | 0.2            |
|                                       | 2.5            | 2.5            | 10.4           |
| Capital assets                        | 13.4           | 12.3           | 12.7           |
| Restricted use funds                  | 0.2            | 0.2            | 0.2            |
| <b>Total</b>                          | <b>\$ 16.1</b> | <b>\$ 15.0</b> | <b>\$ 23.3</b> |
| Bank indebtedness                     | \$ 1.4         | \$ 2.3         | \$ 4.6         |
| Payables and accruals                 | 3.2            | 3.5            | 4.5            |
| Accrued vacation pay                  | 1.2            | 1.3            | 1.6            |
| Deferred contribution                 | 0.3            | 0.6            | 2.3            |
| Current portion of long-term debt     | 0.1            | 0.1            | 0.2            |
|                                       | 6.2            | 7.8            | 13.2           |
| Restricted use funds                  | 0.2            | 0.2            | 0.2            |
| Long-term debt                        | 6.4            | 6.2            | 6.2            |
| Accrued severance pay                 | 2.7            | 3.2            | 3.8            |
| Unamortized portion of capital grants | 6.7            | 6.0            | 6.4            |
| Deficit                               | (6.1)          | (8.4)          | (6.5)          |
| <b>Total</b>                          | <b>\$ 16.1</b> | <b>\$ 15.0</b> | <b>\$ 23.3</b> |

Source: Audited Financial Statements





### 3.28 Peninsulas Health Care Corporation

#### Findings and Recommendations

#### Management Practices

##### 1. Financial Results

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|---------------------------------------|----------------|----------------|----------------|
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| Inventory                             | 0.7            | 0.8            | 0.8            |
| Prepaid expenses                      | 0.1            | 0.2            | 0.2            |
|                                       | 2.5            | 2.5            | 10.4           |
| Capital assets                        | 13.4           | 12.3           | 12.7           |
| Restricted use funds                  | 0.2            | 0.2            | 0.2            |
| <b>Total</b>                          | <b>\$ 16.1</b> | <b>\$ 15.0</b> | <b>\$ 23.3</b> |
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| Current portion of long-term debt     | 0.1            | 0.1            | 0.2            |
|                                       | 6.2            | 7.8            | 13.2           |
| Restricted use funds                  | 0.2            | 0.2            | 0.2            |
| Long-term debt                        | 6.4            | 6.2            | 6.2            |
| Accrued severance pay                 | 2.7            | 3.2            | 3.8            |
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| Deficit                               | (6.1)          | (8.4)          | (6.5)          |
| <b>Total</b>                          | <b>\$ 16.1</b> | <b>\$ 15.0</b> | <b>\$ 23.3</b> |

Source: Audited Financial Statements



### 3.28 Peninsulas Health Care Corporation

The deteriorating financial position is caused by the Corporation spending more than it receives from government and other sources. Figure 3 shows the Corporation's operating results for the years ended 31 March 1998 and 31 March 1999 compared to its budgets and the actual results for the year ended 31 March 1997.

**Figure 3**

**Peninsulas Health Care Corporation  
Operating Results  
For the Years Ended 31 March  
(\$ Millions)**

| Description                         | 1997     | 1998     |         | 1999     |          |
|-------------------------------------|----------|----------|---------|----------|----------|
|                                     | Actual   | Actual   | Budget  | Actual   | Budget   |
| <b>REVENUES</b>                     |          |          |         |          |          |
| Provincial plan                     | \$ 36.0  | \$ 35.8  | \$ 35.7 | \$ 37.3  | \$ 37.3  |
| MCP salaried physicians             | 4.5      | 5.2      | 5.6     | 5.6      | 5.8      |
| Resident revenue                    | 2.2      | 2.2      | 2.3     | 2.2      | 2.3      |
| Other services                      | 1.1      | 1.0      | 0.9     | 1.1      | 0.8      |
| <b>Total Revenues</b>               | 43.8     | 44.2     | 44.5    | 46.2     | 46.2     |
| <b>EXPENDITURES</b>                 |          |          |         |          |          |
| Administration and support          | 15.7     | 14.7     | 14.5    | 15.0     | 15.5     |
| Nursing inpatient services          | 13.0     | 13.9     | 13.5    | 13.9     | 14.4     |
| Medical services                    | 6.1      | 7.2      | 6.3     | 7.7      | 7.3      |
| Diagnostic and therapeutic services | 6.4      | 6.6      | 6.5     | 6.9      | 6.8      |
| Ambulatory care services            | 2.7      | 2.8      | 3.2     | 2.8      | 2.8      |
| Other                               | 0.3      | 0.4      | 0.5     | 0.9      | 1.1      |
| <b>Total Expenditures</b>           | 44.2     | 45.6     | 44.5    | 47.2     | 47.9     |
| <b>NET SHAREABLE ITEMS</b>          | (0.4)    | (1.4)    | -       | (1.0)    | (1.7)    |
| Non-shareable items                 | (0.3)    | (0.9)    | -       | (0.9)    | -        |
| <b>Deficit on operations</b>        | \$ (0.7) | \$ (2.3) | \$ -    | \$ (1.9) | \$ (1.7) |

Source: Audited Financial Statements and Budget.

### 3.28 Peninsulas Health Care Corporation

The deteriorating financial position is caused by the Corporation spending more than it receives from government and other sources. Figure 3 shows the Corporation's operating results for the years ended 31 March 1998 and 31 March 1999 compared to its budgets and the actual results for the year ended 31 March 1997.

**Figure 3**

**Peninsulas Health Care Corporation  
Operating Results  
For the Years Ended 31 March  
(\$ Millions)**

| Description                         | 1997            | 1998            |             | 1999            |                 |
|-------------------------------------|-----------------|-----------------|-------------|-----------------|-----------------|
|                                     | Actual          | Actual          | Budget      | Actual          | Budget          |
| <b>REVENUES</b>                     |                 |                 |             |                 |                 |
| Provincial plan                     | \$ 36.0         | \$ 35.8         | \$ 35.7     | \$ 37.3         | \$ 37.3         |
| MCP salaried physicians             | 4.5             | 5.2             | 5.6         | 5.6             | 5.8             |
| Resident revenue                    | 2.2             | 2.2             | 2.3         | 2.2             | 2.3             |
| Other services                      | 1.1             | 1.0             | 0.9         | 1.1             | 0.8             |
| <b>Total Revenues</b>               | <b>43.8</b>     | <b>44.2</b>     | <b>44.5</b> | <b>46.2</b>     | <b>46.2</b>     |
| <b>EXPENDITURES</b>                 |                 |                 |             |                 |                 |
| Administration and support          | 15.7            | 14.7            | 14.5        | 15.0            | 15.5            |
| Nursing inpatient services          | 13.0            | 13.9            | 13.5        | 13.9            | 14.4            |
| Medical services                    | 6.1             | 7.2             | 6.3         | 7.7             | 7.3             |
| Diagnostic and therapeutic services | 6.4             | 6.6             | 6.5         | 6.9             | 6.8             |
| Ambulatory care services            | 2.7             | 2.8             | 3.2         | 2.8             | 2.8             |
| Other                               | 0.3             | 0.4             | 0.5         | 0.9             | 1.1             |
| <b>Total Expenditures</b>           | <b>44.2</b>     | <b>45.6</b>     | <b>44.5</b> | <b>47.2</b>     | <b>47.9</b>     |
| <b>NET SHAREABLE ITEMS</b>          | <b>(0.4)</b>    | <b>(1.4)</b>    | <b>-</b>    | <b>(1.0)</b>    | <b>(1.7)</b>    |
| Non-shareable items                 | (0.3)           | (0.9)           | -           | (0.9)           | -               |
| <b>Deficit on operations</b>        | <b>\$ (0.7)</b> | <b>\$ (2.3)</b> | <b>\$ -</b> | <b>\$ (1.9)</b> | <b>\$ (1.7)</b> |

Source: Audited Financial Statements and Budget.

### 3.28 Peninsulas Health Care Corporation

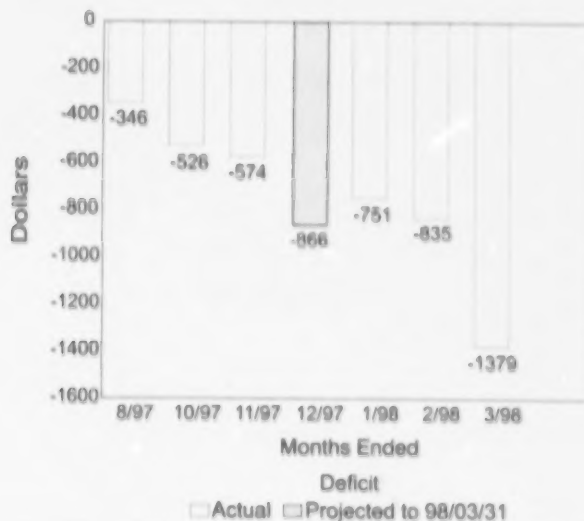
During our audit, we reviewed the 1997-98 fiscal year as this was the most recent full year completed as at the time of our review and updated the 1998-99 financial results subsequent to completion of our audit.

As Figure 3 shows, the Corporation incurred deficits totalling \$1.8 million in health services before non-shareable items in its first two years of operation. In June 1997, which was early in the 1997-98 fiscal year, the Board was aware of its budgetary problems as a deficit of \$1.6 million was projected for the 1997-98 fiscal year. Subsequently, Corporation staff revised the budget after a meeting with the Department of Health in July 1997. The revised budget projected a deficit of \$889,000 for the 1997-98 fiscal year. At that time no further action was taken to reduce the projected deficit of \$889,000 because the Corporation was advised by the Department of Health to wait and see if additional funding would be made available.

In July 1997, the Corporation received additional funding of \$966,000 as its share of the government's \$20 million Health Stabilization Fund. This improved the Corporation's projected financial position for 1997-98 as it eliminated the projected budgetary deficit of \$889,000. However, even though the Department of Health provided this funding to eliminate the projected deficit for 1997-98, the financial reports produced by the Corporation subsequent to this indicated the deficits as disclosed in Figure 4.

Figure 4

Peninsulas Health Care Corporation  
Deficits Per Financial Reports  
1997-98  
(\$ 000's)



### 3.28 Peninsulas Health Care Corporation

With the exception of the projection made in December 1997, there was no other revised deficit projected to 31 March 1998. For the year ended 31 March 1998, the Corporation incurred a deficit of \$1.4 million. This deficit arose from the variances in revenue and expenditures as disclosed in Figure 5.

No action was taken to address the deficit until March 1998 when the Board approved specific cost cutting measures with estimated annual savings of \$675,000. These measures were approved too late to address the deficit for 1997-98.

**Figure 5**

**Peninsulas Health Care Corporation  
Revenue and Expenditure Variances  
For the Year Ended 31 March 1998  
(\$ 000's)**

| Description                 | Budget    | Actual    | Variance   |
|-----------------------------|-----------|-----------|------------|
| Shortfall in revenues       | \$ 44,424 | \$ 44,169 | \$ (255)   |
| Increased costs             |           |           |            |
| Locum travel                | 118       | 259       | (141)      |
| Locum salary                | 2,670     | 3,270     | (600)      |
| Regular salaries            | 27,724    | 28,043    | (319)      |
| Sick leave replacement      | 602       | 868       | (266)      |
| Recruitment                 | 39        | 150       | (111)      |
| Other supplies and services | 10,236    | 10,384    | (148)      |
| Physician salary savings    | 3,036     | 2,575     | 461        |
|                             |           |           | \$ (1,379) |

Source: Peninsulas Health Care Corporation Financial Reports



### 3.28 Peninsulas Health Care Corporation

#### 2. Amounts Owed to the Corporation

Accounts receivable consist of patient receivables, employee receivables, government grants, Harmonized Sales Tax rebates and miscellaneous receivables. As at 31 March 1998, the most recently available audited financial statements, the Corporation was owed \$1.6 million, as shown in Figure 6.

- (a) Included in the Provincial plan receivables - operating for both 1997 and 1998 is \$169,232 related to expenses incurred by the Board when it terminated the employment of a senior executive in January 1997 and hired a replacement in October 1997. Of this amount \$120,155 relates to the termination benefits paid to the former executive. Included in the \$120,155 were payments for benefits not included in Government's normal termination policy. These were payments of \$4,700 for board meetings, \$5,000 for loss of 1997 employment benefits and \$5,000 for financial planning services. In addition, \$15,500 of the \$120,155 was paid directly to the former employees's registered retirement savings plan and not included on any T-4.

Figure 6

#### Peninsulas Health Care Corporation Accounts Receivable For the Years Ended 31 March

| Account Receivable                        | 1997                | 1998                |                                       |                     |
|-------------------------------------------|---------------------|---------------------|---------------------------------------|---------------------|
|                                           | Net<br>Receivable   | Total<br>Receivable | Allowance<br>for Doubtful<br>Accounts | Net<br>Receivable   |
| <b>Operating</b>                          |                     |                     |                                       |                     |
| Provincial plan                           | \$ 539,076          | \$ 241,884          | \$ 0                                  | \$ 241,884          |
| Insurance plans & individuals             | 291,721             | 442,352             | 66,071                                | 376,281             |
| MCP                                       | 6,948               | 666,718             | 385,372                               | 281,346             |
| Sundry                                    | 589,081             | 207,127             | 0                                     | 207,127             |
| <b>Capital</b>                            |                     |                     |                                       |                     |
| Provincial plan                           | 165,000             | 308,200             | 0                                     | 308,200             |
| Sundry                                    | 4,990               | 0                   | 0                                     | -                   |
| <b>Other</b>                              |                     |                     |                                       |                     |
| Cottage complexes                         | 63,309              | 158,614             | 0                                     | 158,614             |
| Burin Peninsula Health Care<br>Foundation | 73,520              | 1,351               | 0                                     | 1,351               |
| <b>Total</b>                              | <b>\$ 1,733,645</b> | <b>\$ 2,026,246</b> | <b>\$ 451,443</b>                     | <b>\$ 1,574,803</b> |

Source: Corporation's financial records

### 3.28 Peninsulas Health Care Corporation

- (b) Our review of the most recently aged receivables from insurance plans and individuals indicated that, as at 31 December 1998, these receivables totaled \$436,900. As Figure 7 indicates, \$269,351 of this amount related to accounts maintained by the Clarenville accounting system while the remaining \$167,549 related to accounts maintained by the Burin accounting system.

The Corporation's patient receivables continue to increase. In addition, \$284,819 or 65% of the receivables are more than 60 days old. The Corporation has made efforts to collect its receivables through a collection agency; however, of the \$28,602 submitted to the Corporation's collection agency, only \$1,926 or 7% has been collected.

- (c) Sundry receivables of \$207,127 consist of the following:

| Description                  | Amount            |
|------------------------------|-------------------|
| Employee payroll receivables | \$ 15,002         |
| Travel advances              | 5,186             |
| Harmonized Sales tax rebates | 114,793           |
| Miscellaneous                | <u>72,146</u>     |
|                              | <u>\$ 207,127</u> |

Figure 7

#### Peninsulas Health Care Corporation Aged Accounts Receivable 31 December 1998

| Ageing        | Clarenville |         | Burin      |         | Total      |         |
|---------------|-------------|---------|------------|---------|------------|---------|
|               | Amount      | Percent | Amount     | Percent | Amount     | Percent |
| Current       | \$ 57,748   | 21%     | \$ 33,213  | 20%     | \$ 90,961  | 21%     |
| 31 to 60 days | 30,109      | 11%     | 31,011     | 18%     | 61,120     | 14%     |
| 61 to 90 days | 29,162      | 11%     | 21,445     | 13%     | 50,607     | 11%     |
| Over 90 days  | 152,332     | 57%     | 81,880     | 49%     | 234,212    | 54%     |
| Total         | \$ 269,351  | 100%    | \$ 167,549 | 100%    | \$ 436,900 | 100%    |

Source: Corporation's aged accounts receivable listings 31 December 1998

### 3.28 Peninsulas Health Care Corporation

- (d) Of the \$158,614 due from the cottage complexes for reimbursement of cottage administrative costs, \$63,309 relates to the 1996-97 fiscal year and \$95,305 relates to the 1997-98 fiscal year. As of the date of our audit, January 1999, these amounts had not been transferred to the Corporation's operating account which is in an overdraft position. Therefore this amount is not available to meet the cash flow requirements of the Corporation.

#### 3. Accountability

Public accountability holds to the premise that stakeholders are best served by knowing whether the most important management responsibilities conferred on agencies of the Crown are satisfactorily carried out and that the intended results are achieved. A complete system of accountability commences with the strategic planning phase, leading to development of operational plans, the delivery of the programs and finally to reporting on the achievement of the objectives. Government has recently approved an accountability framework for agencies of the Crown, including health care boards.

The Corporation has completed its strategic planning phase and is in the process of developing its operational plan. In addition, it has prepared performance related documents such as an annual report for 1997-98 and a Report Card. This is a good start to the development of an accountability framework and the Board should continue with its efforts in this area.

We reviewed the Corporation's Annual Report for 1997-98 and its Report Card and offer the following suggestions:

- The Annual Report should identify the Corporation's objectives and its performance in comparison to these objectives.
- The Annual Report gives some statistical information such as length of stay, patient days and surgeries. The Report would be improved if there was a comparison of this information to benchmarks and if information on the cost of the services provided by the Corporation was also included. The Corporation should interpret this information and include this in the Report.
- The Annual Report includes a copy of the balance sheet and statement of revenue and expenditure; however, commentary should be provided to interpret this information for readers. In addition, the Corporation's financial results should be compared to its original budget.

### 3.28 Peninsulas Health Care Corporation

- In December 1998 the Corporation prepared a Report Card comparing certain information to benchmarks; however, this Report Card has not been provided to stakeholders including patients, members of the community, the Department of Health and the House of Assembly.

#### Purchasing

##### 1. *Public Tender Act*

For the year ended 31 March 1998 the Corporation spent approximately \$11.7 million on goods and services. Our examination in this area included a review for compliance with the *Public Tender Act*. At the time of our review, the *Public Tender Act* required the Corporation to publicly tender for goods and services estimated to cost more than \$7,500 and where tenders were not required to be invited, to obtain prices either from at least three legitimate suppliers by direct quotation, by other means that the Corporation considers advisable, or establish for the circumstance a fair and reasonable price for the goods and services.

Our review of a random sample of 14 purchases greater than \$7,500 totalling \$659,000 disclosed that 13 of these purchases complied with the *Act* while for one purchase there was no documentation to determine if the purchase was in compliance with the *Act*. This purchase was for the quarterly payment of \$10,453 on a five year maintenance agreement expiring 31 March 1999 for the heat automation system in Burin and temperature control installation at the St. Lawrence Medical Clinic. This agreement was signed prior to the current Board's existence and no documents were available to determine if the purchase was made in compliance with the *Act*.

Out of the eight purchases that were publicly tendered our review identified the following:

- Three tender requests made reference to brand names in the specifications. Guidelines prepared by the Department of Health which are to be used in acquiring medical equipment explicitly state that "*Specific manufacturers' and/or models should not be mentioned as this will limit competition.*" The successful bidders were the bidders supplying the specified models at a combined value of \$71,910.

### 3.28 Peninsulas Health Care Corporation

- One tender for chemistry and hematology equipment and supplies resulted in a purchase costing \$105,126 per year for seven years. However, one potential bidder indicated that only one supplier could meet the tender specifications as the requested test capacity exceeded all other suppliers and far exceeded the Corporation's requirements. The specifications required a capacity of 1,050 tests/hour while the average for the particular hospital was 650 tests/day. If the equipment was used to its full potential, it could do all the daily tests in one hour.

#### 2. Capital Assets

As at 31 March 1998, the Corporation reported capital assets of \$29.4 million as indicated in Figure 8.

Our review of physical and accounting controls over capital assets identified the following:

- There is no capital asset ledger or listing that identifies individual assets by serial number or asset number. The Corporation does maintain listings of annual additions to capital assets; however, these listings do not identify assets individually. As a result, we could not determine what assets are included in the cost amounts reflected in Figure 8 nor could we verify that all capital assets purchased by the Corporation were still on hand.

Figure 8

**Capital Assets**  
**31 March 1998**  
**(\$000's)**

| Asset                      | Cost             | Accumulated Depreciation | Net Book Value   |
|----------------------------|------------------|--------------------------|------------------|
| Land and land improvements | \$ 231           | \$ 22                    | \$ 209           |
| Buildings                  | 13,284           | 6,086                    | 7,198            |
| Equipment                  | 15,680           | 10,786                   | 4,894            |
| Vehicles                   | 156              | 146                      | 10               |
|                            | <b>\$ 29,351</b> | <b>\$ 17,040</b>         | <b>\$ 12,311</b> |

Source: Audited Financial Statements





### 3.28 Peninsulas Health Care Corporation

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|                            | <b>\$ 29,351</b> | <b>\$ 17,040</b>         | <b>\$ 12,311</b> |

Source: Audited Financial Statements

### 3.28 Peninsulas Health Care Corporation

- Capital assets are not tagged, recorded and counted annually. Corporation staff indicated that the Information Technology Department attempted to tag and inventory all of the computers and related hardware in 1997; however, this information was lost when the computer system being used failed. The Corporation did not back up the database, or retain any reports or input documents which would have allowed it to recover from this failure.
- As a result of the significant investment in equipment and the requirement to provide uninterrupted health care services, it is necessary to maintain a record of each significant piece of equipment and the repairs and maintenance made to each to ensure that all equipment is properly maintained and that information required for equipment replacement is readily available. At the time of our audit, January 1999, the Corporation did not have a centralized database of repairs and maintenance relating to each significant piece of equipment to ensure all Corporation equipment is properly maintained.

The Corporation has contracted a biomedical company to maintain essential medical equipment. This company submits a report on the service performed on each piece of equipment; however, there is no database to record and monitor this information and other maintenance contracts to ensure they are kept current and that all pieces of equipment which have a maintenance contract are properly maintained. We were informed that reliance is placed on each individual site to ensure that the equipment is properly maintained and appropriate contracts are in place.

- The Corporation has nine vehicles which are used for general purposes, supply transportation, maintenance and patient transportation. Mileage log books are not maintained for any of the vehicles. In addition, the Corporation could not readily tell us the operating costs of these vehicles either individually or in total. Without this information, the Corporation cannot properly monitor the cost and usage of its vehicles.
- During 1997-98, the Corporation maintained 49 housing units for salary and locum physicians. Salary physicians are permanent employees of the Corporation while locum physicians are temporary replacement physicians who are paid on an hourly or daily basis. The Corporation owned 15 units with operating costs, excluding depreciation and net of rental revenues, of \$74,022 in 1997-98. In addition, the Corporation rented another 34 units with operating costs, net of rental revenues, of \$178,010 in 1997-98.

### 3.28 Peninsulas Health Care Corporation

The Corporation has separate general ledger accounts for each of the 49 properties and our review of these accounts disclosed that Corporation-owned units cost up to \$11,000 per year, excluding depreciation and net of rental revenue, to operate while rented units cost up to \$17,000 per year, net of rental revenue. Locum and some salary physicians are accommodated free of charge while other physicians pay rent of \$500 to \$550 per month in the Clarenville area. For the year ended 31 March 1998, the Corporation subsidized housing costs by \$252,032, excluding depreciation.

For the year ended 31 March 1998, the Corporation sold 4 of its 15 housing units for \$312,904. These houses originally cost \$357,629 and had a net book value of \$297,773. Corporation staff indicated that it is the Corporation's intention to sell all of the housing units if a market becomes available and rent units where needed. However, there was no cost-benefit analysis carried out on the Corporation owned houses to determine whether the disposition of these properties would reduce housing costs and/or provide other benefits to the Corporation.

• Golden Heights Manor was originally opened in September 1977 as a 47 bed nursing home for the Bonavista area. It cost approximately \$900,000. In 1987 the Manor was extended by a 40 bed addition at a cost of \$4,000,000. The residents of the older section were then transferred to the new extension. In the earlier 1990's the old section was renovated and the previous 47 bed section were converted to 30 modern units. The total capacity of the Manor was now 70 beds; however, only 60 beds were ever utilized. The Corporation indicated that there was no demand for the additional beds. Our review of the waiting list from December 1997 to July 1999 supported this assertion as there was no one on the list from December 1997 to April 1998. The waiting list for the period May 1998 to July 1999 was as follows:

| Month          | Waiting List | Month         | Waiting List |
|----------------|--------------|---------------|--------------|
| May 1998       | 3            | January 1999  | 2            |
| June 1998      | 0            | February 1999 | 4            |
| July 1998      | 4            | March 1999    | 4            |
| August 1998    | 3            | April 1999    | 4            |
| September 1998 | 4            | May 1999      | 3            |
| October 1998   | 10           | June 1999     | 3            |
| November 1998  | 6            | July 1999     | 3            |
| December 1998  | 0            |               |              |

### **3.28 Peninsulas Health Care Corporation**

#### **3. Inventory**

As at 31 March 1998, the Corporation reported \$769,000 in inventory consisting of \$546,000 in medical, surgical and other supplies and \$223,000 in drugs. The Corporation has major inventory sites in Clarenville, Bonavista and Burin. The Corporation has a Director of Materials Management with a staff of five in Clarenville and four in Burin.

The Corporation has two separate computerized inventory systems which were used previously by the two former hospital boards. The Meditech system is used to account for the inventories at the Burin site while the Computer-Ease system is used to account for the inventories at the Bonavista and Clarenville sites. In each of these systems there are differing policies and procedures, information reporting formats and inventory requisition forms. As a result, the Corporation is incurring additional costs to maintain two systems and there is the possibility of inconsistencies occurring in the controlling and reporting of these inventories.

Inventory counts are only formally conducted and recorded once a year for year-end accounting purposes. Periodic test counts of the actual inventories are not conducted and agreed to the inventory records. As a result, discrepancies are usually detected only at year end.

Drug inventories on the computer system at the Clarenville site are not updated on a timely basis. Drugs removed from the shelves are recorded on patient medication profiles and these are not recorded on the computerized system until the patient is discharged or at year end. The Corporation maintains a manual ledger, as required by legislation, and a computerized system for restricted drugs. Periodic test counts are conducted on restricted drugs. The results of the test counts are agreed to the control sheet but not to the computerized listing. During our review a test count of a sample of 14 drugs and the comparison to the computerized listing disclosed three exceptions; however, a comparison to the manual control sheets identified no exceptions.

#### **4. Significant Expenditures**

Our examination included an analytical review of all expenditure accounts to identify significant expenditures. This review disclosed the following:

- The Corporation's 1997-98 travel costs of \$784,000 exceeded the budget of \$505,000 by \$279,000. Most of the excess expenditures were in the areas of locum travel and recruitment expenses. Locum travel costs exceeded the budget by approximately \$141,000 (actual expenditures of \$259,000 compared to a budget

### 3.28 Peninsulas Health Care Corporation

of \$118,000) while recruitment and relocation costs exceeded the budget by \$111,000 (actual expenditures of \$150,000 compared to a budget of \$39,000).

A detailed review of certain travel claims disclosed three instances where an employee approved their own travel claims. In addition, travel claims do not always indicate the time of departure and return and, as a result, the Corporation cannot determine if the proper amounts are claimed for less than full day travel.

- Government relocation policy permits the reimbursement of legal fees resulting from the purchase of another dwelling at the place of relocation provided such fees are incurred within one year of relocation. The Corporation reimbursed one senior employee \$2,252 for legal fees on the purchase of a house two years after the employee was relocated.
- Telephone long-distance charges of \$142,000, exceeded budget of \$122,000 by \$20,000. Employees are not required to log long-distance calls making it difficult, if not impossible, to tell if the calls were for business. Most of the \$50,000 for long-distance charges at the Clarendville hospital are being charged to one general ledger account and not to individual departments where managers would have to account for this expenditure. In addition, since 1 November 1997, the Corporation's long-distance service provider billed in electronic format; however, the Corporation is unable to read this information. As a result, long distance telephone calls are approved and payment is made without verifying that the charges are bona fide expenditures of the Corporation.
- The Corporation maintains two separate financial systems. The Corporation's main system is located in Burin, 188 km from its headquarters in Clarendville. The supporting documentation for all transactions that are entered into the Burin system is kept in Burin while a second accounting system is used at the headquarters in Clarendville. Supporting documentation for the second system is kept in Clarendville. Data from the Clarendville system is then transferred to Burin where it is merged into its system to provide the complete reports. In addition to the duplicate time and costs to maintain the two financial systems, corporate audit fees of \$30,000 exceeded budget of \$15,000, by \$15,000.

### 3.28 Peninsulas Health Care Corporation

#### Human Resources

Employee salaries and benefits are the largest expenditures of the Corporation accounting for \$34.7 million or 76% of the total shareable expenditures of the Corporation in 1997-98. As of April 1998, the Corporation reported having 692 budgeted full-time equivalent positions and 787 paid full-time equivalent positions. The paid full-time equivalent positions include part-time, temporary and casual staff. Figure 9 provides a breakdown of the Corporation's staffing complement by site.

Figure 9

**Peninsulas Health Care Corporation  
Staff Complement - Full Time Equivalent Positions  
April 1998**

| Description                        | Management | Union  | Salaried Physicians | Other | Total  |
|------------------------------------|------------|--------|---------------------|-------|--------|
| Budgeted full-time equivalent      | 48.00      | 595.00 | 49.00               | -     | 692.00 |
| <b>Paid full-time equivalent</b>   |            |        |                     |       |        |
| Dr. G.B. Cross Memorial Hospital   | 11.00      | 205.08 | 10.00               | 7.00  | 233.08 |
| Bonavista Hospital                 | 2.00       | 60.72  | 3.00                | 1.00  | 66.72  |
| Golden Heights Manor               | 2.00       | 71.56  | -                   | 3.00  | 76.56  |
| Burin Peninsula Health Care Centre | 18.75      | 206.44 | 9.69                | 7.00  | 241.88 |
| Blue Crest                         | 3.75       | 80.72  | -                   | 1.25  | 85.72  |
| U.S. Memorial Health Care Centre   | 2.00       | 56.89  | 1.40                | 1.50  | 61.79  |
| Grand Bank Community Health Centre | -          | 14.93  | 4.00                | -     | 18.93  |
| Clinics                            | -          | 1.33   | 1.00                | -     | 2.33   |
| Total paid full-time equivalent    | 39.50      | 697.67 | 29.09               | 20.75 | 787.01 |

Source: *Questions and Answers* May 1998 and Peninsulas Health Care Corporation's Human Resources Department.



### 3.28 Peninsulas Health Care Corporation

#### Human Resources

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| <b>Paid full-time equivalent</b>       |              |               |                     |              |               |
| Dr. G.B. Cross Memorial Hospital       | 11.00        | 205.08        | 10.00               | 7.00         | 233.08        |
| Bonavista Hospital                     | 2.00         | 60.72         | 3.00                | 1.00         | 66.72         |
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| Grand Bank Community Health Centre     | -            | 14.93         | 4.00                | -            | 18.93         |
| Clinics                                | -            | 1.33          | 1.00                | -            | 2.33          |
| <b>Total paid full-time equivalent</b> | <b>39.50</b> | <b>697.67</b> | <b>29.09</b>        | <b>20.75</b> | <b>787.01</b> |

Source: *Questions and Answers* May 1998 and Peninsulas Health Care Corporation's Human Resources Department.

### 3.28 Peninsulas Health Care Corporation

#### 1. Human Resources Planning

For the past two years, the Corporation has experienced shortages of physicians in the region. In July 1997, the Corporation reported 20 physician vacancies while one year later in July 1998 there were 16 physician vacancies. The majority of vacancies occurred in casualty officers (emergency room doctors). The Board has taken on some initiatives with the Department of Health, including the payment of physicians for their services as emergency doctors at \$80 per hour. Also, the Corporation provides a housing allowance to physicians to attract them to the area. Due to the shortage of physicians in the region, the Corporation has had to rely heavily upon temporary replacement physicians known as locum doctors to provide the necessary level of health care.

For the year ended 31 March 1998, the cost of replacing salaried doctors (locum costs) was \$3.5 million, which exceeded the \$2.8 million budget by \$0.7 million. Figure 10 provides a breakdown of the locum costs compared to regular physician costs.

Figure 10

**Peninsulas Health Care Corporation  
Physician Costs  
For the Year Ended 31 March 1998  
(\$ 000's)**

| Hospitals                              | Locum Costs |        |          |          | Regular Physicians |          |
|----------------------------------------|-------------|--------|----------|----------|--------------------|----------|
|                                        | Salaries    | Travel | Total    | Budget   | Salaries           | Budget   |
| Burin Peninsula Health Care Centre     | \$ 943      | \$ 50  | \$ 993   | \$ 648   | \$ 1,101           | \$ 1,327 |
| US Memorial Health Care Centre         | 412         | 43     | 455      | 124      | 40                 | 307      |
| Grand Bank Community Health Centre     | 178         | 23     | 201      | 213      | 394                | 433      |
| G.B. Cross Memorial Hospital           | 1,030       | 79     | 1,109    | 1,398    | 843                | 776      |
| Bonavista Peninsula Health Care Centre | 707         | 63     | 770      | 404      | 197                | 193      |
| Total                                  | \$ 3,270    | \$ 258 | \$ 3,528 | \$ 2,787 | \$ 2,575           | \$ 3,036 |

Source: Peninsulas Health Care Corporation Financial Records

### 3.28 Peninsulas Health Care Corporation

Of the \$3.3 million paid to replacement doctors for salaries, \$2.8 million is recoverable through MCP while the remaining \$0.5 million must come from the Corporation's operating grant.

#### 2. Employee Leave

At the time of our review, the Corporation had separate leave systems for Clarenville and Burin. The Clarenville system recorded both long-term and short-term sick leave separately while the Burin system grouped both together. Corporation policy requires that leave forms be used to approve leave; however, the biweekly payroll time sheets were used to record this information in the year-to-date leave systems. A review of the controls and monitoring of leave at the Corporation indicated the following:

- In 1997-98 sick leave replacement costs were budgeted at approximately \$600,000; however, actual costs were \$882,000, exceeding budget by 47%. Figure 11 summarizes the Corporation's sick leave statistics for the past two fiscal years:
- Employee leave was not always supported by approved leave forms. Our review of a sample of 23 periods of employee leave indicated that 15 had leave forms filed, 1 had correspondence on file to support the leave and 7 had no forms to support the leave. Without proper supporting documentation leave could be recorded incorrectly and disputes could arise over leave taken.

Figure 11

#### Peninsulas Health Care Corporation Sick Leave Analysis For the Fiscal Years

|                          | 1997-98      | 1996-97      | Variance   |
|--------------------------|--------------|--------------|------------|
| Sick leave hours         | 90,935.6     | 87,522.5     | 3,413.1    |
| Sick leave costs         | \$ 1,374,555 | \$ 1,246,002 | \$ 128,553 |
| Replacement costs        | \$ 881,851   | \$ 857,954   | \$ 23,897  |
| Total cost               | \$ 2,256,407 | \$ 2,103,956 | \$ 152,451 |
| FTE's                    | 785.00       | 759.26       | 25.74      |
| Total cost per FTE       | \$ 2,875     | \$ 2,771     | \$ 104     |
| Sick leave hours per FTE | 115.80       | 115.30       | 0.50       |

Source: Peninsulas Health Care Corporation's Human Resources Department's sick leave statistics

### 3.28 Peninsulas Health Care Corporation

- A review of the 31 December 1997 leave balances for one hospital indicated that nine employees had credit balances in their sick leave accruals ranging from 15.36 hours to 89.1 hours. Also, 24 employees had credit balances in their annual leave balances ranging from 0.25 hours to 202 hours. Corporation policy allows employees to credit their annual leave banks a maximum of three days under certain conditions and their sick leave banks a maximum of 15 days if all other sick leave credits have been exhausted. This is not consistent with Government policy which does not allow employees to overdraw their leave balances.
- We also traced five employee leave forms back to the year-to-date reports to ensure the completeness of postings. One leave form showed time taken off as annual leave; however, it was posted to the year-to-date attendance report as sick leave. The error was corrected after it was brought to the attention of the Human Resources Department.
- Many employees, mostly nurses, are required to notify their department upon sick leave for shift relief purposes. A Notification of Sick Leave form is completed, over the phone, which includes the employee's name, department, date and time of call, date and shift to be covered and who received the call. This form is forwarded to Human Resources and is used to support the sick leave. This form, however, is not approved by the employee's supervisor nor is it signed by the employee.

### 3. Staffing

A major responsibility of the Corporation is the hiring and evaluation of staff. During 1997, the Corporation held 184 competitions; approximately 85% of which were internal competitions. Our review of the staffing function indicated the following:

- The Corporation maintains a log book of all competitions and files an employment authorization sheet along with the job posting with the book. A review of a sample 3 of 27 external competitions indicated that competition files are maintained numerically and include applications, interview questions, interview notes, appointment letters, and summary competition sheets. However, there was no documentation of the ranking process of final candidates or reference checks although the Director of Human Resources stated reference checks are always performed.

### 3.28 Peninsulas Health Care Corporation

- The Corporation's draft policy on reviews of staff performance requires that probationary reviews are to be conducted once an employee's probationary period is complete and that subsequent annual performance reviews are to be conducted. The Director stated that the Corporation conducted a review six months previous to our review which concluded there was a 40% compliance rate with the performance review policy. Based upon this, we reviewed a limited sample of six existing employees; three long-term employees and three employees hired in 1997. Of the three long-term employees, one employee was last reviewed in April 1997, one in June 1996 and the other in August 1995. The three new employees had orientations performed; however, there was no evidence of any probationary review or any other performance review.

#### Recommendations

*The Corporation should:*

- *take steps to address the increasing operating deficit;*
- *include performance objectives and related outcomes as part of its Annual Report to stakeholders;*
- *encourage competition in the tendering process rather than limiting competition by references to specific equipment brands and too stringent specifications;*
- *develop and implement standard controls over its capital assets and inventories;*
- *ensure its competition files are complete and include all documentation to support a competition;*
- *ensure performance reviews are conducted according to Corporation policy; and*
- *continuously report on and monitor the level of sick leave within the Corporation and ensure that leave forms are properly completed, filed, approved and cross-referenced to the year-to-date attendance reports.*



### 3.28 Peninsulas Health Care Corporation

#### Corporation's Response

##### Management Practices

##### 1. Financial Results

*The Corporation did make a projection of its deficit to March 31, 1998 in December 1997. This projection was presented to the Department of Health and Community Services. The response received was to make whatever reductions possible in discretionary spending but to not reduce patient/resident care activity. The Department subsequently informed the Board that a budgetary review would be undertaken for all institutional health care boards. The review for this Board occurred in June 1999 for fiscal year 1998/99.*

*The growing deficit has been a concern of the Board of the Peninsulas Health Care Corporation and this has been communicated to the Department of Health and Community Services. Your report indicates an accumulated deficit of \$8.4 million. This includes accruals for vacation pay and severance pay which is only funded on a cash basis. The actual accumulated deficit for government reporting which you reviewed as part of the audited financial statements was \$3.9 million determined as follows:*

|                                                     |                             |
|-----------------------------------------------------|-----------------------------|
| <i>Accumulated deficit per your report</i>          | <i>\$8.4 million</i>        |
| <i>Less: Accrued vacation pay</i>                   | <i>1.3 million</i>          |
| <i>Accrued severance pay</i>                        | <i><u>3.2 million</u></i>   |
| <i>Accumulated deficit for government reporting</i> | <i><u>\$3.9 million</u></i> |

*In the following fiscal year, 1998/99, the Department of Health and Community Services provided \$3,868,000 towards this accumulated deficit. This funding also had a significant positive effect on cash flow for the Corporation.*

*With respect to the operating deficit for the Corporation we did receive funding in 1998-99 to cover the bulk of our deficit up to March 31, 1999. Since this adjustment was not received until early 1999 we recorded an operating deficit of \$1.9 million to 31 March 1999. Had this money been received prior to March 31, 1999 our operating deficit would have been approximately \$35,000.*

*The Corporation is still experiencing operating deficit and is awaiting a response from the Department on the budget submission for 1999/2000.*



### **3.28 Peninsulas Health Care Corporation**

#### **2. Amount owed to the Corporation**

- (a) *This receivable has been collected from the Department of Health and Community Services. An amended T4 has been issued for the amount paid directly to the former employee's registered retirement savings plan. Again we would like to emphasize that the receivables referred to here - former employee - were all approved by the Department of Health and Community Services and have been collected from the Department.*
- (b) *The turnaround time for collection of patient receivables is often in excess of 60 days. The Corporation has a policy of sending amounts over 120 days to a collection agency and so far these efforts are not generating significant collections. The allowance for non-collectibles was increased for 1998/99.*

#### **3. Accountability**

*Your comments related to accountability are valid and your suggestions for improvements to the annual report of the Corporation will be taken into consideration when preparing the next annual report.*

*I am pleased to advise that the Board has gone through two strategic planning processes in the past two years. This process has resulted in the completion of a Strategic Plan (already submitted to your office). This plan was reviewed again in October 1999 and new strategic directions agreed to.*

*The increasing operating deficit is indeed a concern of the Board of the Peninsulas Health Care Corporation. For fiscal years 1998/99 and 1999/2000, detailed budgets were prepared and presented to the Department of Health and Community Services projecting deficits.*

*The Board requires additional operating funds in order to maintain and enhance the service it has been mandated to provide. Therefore, the deficit will continue to increase or services will have to be reduced. There is no ability to make further discretionary reductions. To date the Department of Health and Community Services has advised the Corporation to not reduce services.*

*The recommendation that the Board should include performance objectives and related outcomes as part of its Annual Report to stakeholders will be considered.*

### **3.28 Peninsulas Health Care Corporation**

#### ***Purchasing***

##### ***1. Public Tender Act***

*In each of the tenders, although specific models were referenced, it was not the intent to limit competition. This is borne out by the addition of "or equivalent" alongside the model specified. On page 25 of the Guidelines, (8.3.1.1 NOTE) clarification is provided to the statement that 'mention of a model may eliminate the need for tendering'. This is obviously not the intent in our three tenders, as the "or equivalent" statement will attest. The fact that more than one bid was received for each of the three tenders further confirms that competition was not limited. Under the Public Tender Act, the low bid that meets minimum specifications MUST be accepted, and in all cases this was done.*

*As a point of information, the "Guidelines" referenced have not been adopted as Government policy as indicated in the Preface, Page vii. It is suggested, however, that they be considered as representing recommended practice. Even if the Guidelines were policy, it does not mean that there was a violation for the three tenders referenced. The model was used for reference only of our requirements.*

##### ***2. Capital Assets***

*The Corporation has commenced a project to identify and record all of its capital assets. The assets will be identified by location, tagged, costed and accounted for in a capital asset sub-ledger. In addition, policies relating to capital assets, purchase and disposition are being reviewed. So far the assets at Burin Peninsula Health Centre, U.S. Memorial Health Care Centre, Grand Bank Community Health Centre, and Blue Crest Inter Faith Home have been identified and inventoried. A regional computerized sub-ledger system to record assets has yet to be purchased and installed.*

*The Corporation has purchased a preventative maintenance system for use in facilities management to maintain records of each significant piece of equipment in the Corporation. This will allow for a centralized database of repairs and maintenance to each such piece of equipment.*

*The Corporation has also assigned the responsibility for maintenance service contracts to one individual. We can utilize the recently implemented Materials Management system to record all service contracts in the Corporation.*

### **3.28 Peninsulas Health Care Corporation**

*The issue you raised with respect to the vehicles is now being addressed by the Corporation. The vehicles are located in several of the Corporation's sites and are presently the responsibility of several departments. It is the intention of the Corporation to now assign the responsibility of maintaining the vehicles to Facilities Management which has a presence at all sites. Responsibility for mileage logs and expenses will be part of the management of the vehicles.*

*When the Corporation was formed in January 1996, the Board decided to sell physicians houses that were owned by the Corporation. In addition to the operating costs associated with the houses there is significant time and effort required by facilities staff and other staff for their maintenance.*

*The Corporation acknowledges the changes to Golden Heights Manor Nursing Home. However, these changes were completed almost 10 years prior to the formation of the Peninsulas Health Care Corporation. As stated in Note 1 to the Consolidated Financial Statements, the Peninsulas Health Care Corporation assumed all assets and liabilities of several other boards including the Bonavista Peninsula Board. At present, there is no demand to open the remaining 10 beds.*

#### **3. Inventory**

*It is correct that two computerized inventory systems have been in place at the Corporation, one at the Dr. G. B. Cross Memorial Hospital and one at the Burin Peninsula Health Centre. This problem has been eliminated with the implementation of the Meditech system at both sites.*

*Inventory records at the Dr. G. B. Cross Memorial Hospital have been kept in Materials Management of all medical, surgical and other supplies that are in inventory. Supplies are recorded when received and issued to users then recorded and updated monthly. However, certain supplies are issued to nursing unit using a cart system which is not an official inventory. With the implementation of the regional inventory system, changes are being made so that suggested departmental inventories are also maintained.*

*The inventory system for drugs at the Dr. G. B. Cross Memorial Hospital is also being replaced with the new Meditech System. This will provide the Corporation with a better recording system for drugs received and issued. It will also provide regional consolidated information.*

### 3.28 Peninsulas Health Care Corporation

#### 4. Significant Expenditures

*During 1997/98 the Corporation had many vacancies in the medical staffing complement. The Corporation was also active in its recruitment of physicians. This situation did result in excessive locum requirements which resulted in significant travel costs since these locums traveled from outside the region. As recruitment efforts became successful, recruitment and relocation costs also increased. While the variances were high, the Corporation was able to continue to provide services to all patients and residents in the region.*

*The Corporation continues to incur costs for medical services over and above what we get reimbursed for from MCP/DOHCS. (We did get reimbursed for this expense in 1998-99 as part of the total settlement.) The Corporation's success in medical recruitment has improved dramatically in the last two years. At present we have only 4 vacancies - all for which we have physicians being recruited. The additional costs incurred for locum coverage during the time of your review were unavoidable. The alternate to this would have been service interruptions - a situation which was intolerable to the Board, the Department of Health and Community Services and the public.*

*With respect to the legal fees for a senior employee on the purchase of a dwelling, the Board of the Corporation had agreed to this payment at the time of hiring the employee. While the purchase of the dwelling did occur after the one year, the commitment had already been made.*

*The Corporation is starting to implement an authorization code system for long distance calls. So far, the supplier of long distance has not been able to provide the Corporation with such a system. Improvements are indeed required to long distance calls including the charging to departments and verification. The new system should help this effort.*

*In March 1999, the Corporation started an implementation process to regionalize its information systems. The system purchased is the Meditech software. To date, accounts payable, materials management, and general ledger are implemented. Payroll/personnel will be regionalized by November 1999 and billing/accounts receivables will be live by March 2000. This will significantly improve the various components of the financial information system for the Corporation.*

*The Board does encourage competition in the tendering process and does not limit competition. The Board is supportive of public tendering and many goods and services are tendered.*

### 3.28 Peninsulas Health Care Corporation

*The efforts to develop and implement standard controls over capital assets and inventories are well under way at the Corporation. These efforts include:*

- *Regionalization of inventory and purchasing with the implementation of the Meditech system in July 1999.*
- *Capital assets at Burin site have been inventoried. A software system for tracking capital assets will be purchased and implemented regionally. The whole project should be completed by December 2000.*

#### ***Human Resources***

*The outlined recommendations are appropriate but it is not practical to comply with specific items.*

*The sick leave notification form is not being used as a control system. It is used for notification purposes only and therefore is not always signed.*

*The leave request form is an authorization for leave. The Department Time Sheets are signed off by the appropriate person and would be authorization for time worked and leave taken. As we are moving to an electronic format it would not seem appropriate to utilize additional resources to reconcile all leave request forms.*

*However, Human Resources will comply with recommendations by putting necessary controls in place to monitor the process for leave and sick leave.*

*The Corporation is embarking upon an Attendance Management Program. Our sick leave is not the highest in the province, however, we recognize that efforts have to be made to achieve improvements.*



### **3.29 Health and Community Services Boards**

#### **Introduction**

On 1 April 1998, Government transferred programs for community services from the Department of Human Resources and Employment to the Department of Health and Community Services. Effective this same date, Government directed that community service programs including Child Welfare, Community and Corrective Services and Family Rehabilitative Services, be integrated and delivered under the health and community services boards.

There are four health and community services boards in the Province comprised of St. John's, Eastern, Central and Western regions. Each of these boards has local offices throughout the Province. Health and Community Services in northern Newfoundland and in Labrador are administered as separate components of the Grenfell Regional Health Services Board and the Health Labrador Corporation.

In addition to the programs transferred from the Department of Human Resources and Employment on 1 April 1998, the health and community services boards provide traditional community health services including health promotion and protection, mental health, continuing care and immunization services.

Community service programs that were designated for transfer on 1 April 1998 from the Department of Human Resources and Employment to the Western Regional Health and Community Services Board and to the Health Labrador Corporation were not transferred until 1 April 1999. For the 1998-1999 year, these community service programs were administered directly by the Department of Health and Community Services.

#### **Conclusion**

The financial position and operating results of the four health and community services boards deteriorated significantly in 1998-99. For example, deficits after non-shareable expenses in 1998-99 totalled \$8.7 million before additional funding of \$2.3 million was provided by Government in April 1999. In 1997-98, the four boards reported a net surplus after non-shareable expenses of \$1.2 million. Furthermore, total net assets of the four boards decreased from \$5.4 million in 1997-98 to \$1.5 million in 1998-99.

In addition, the four boards are projecting deficits totalling \$11.8 million for 1999-2000. This \$11.8 million does not include increases in severance and vacation pay which are expected to further increase the deficits. The Department has committed to providing additional funding of \$4.0 million to help fund these deficits which will effectively decrease the projected deficits to \$7.8 million.



### 3.29 Health and Community Services Boards

#### Findings

As part of the on-going work of our Office, we review the financial statements and other information of the health and community services boards. Our review in 1999 included an assessment and comparison of the financial results and the financial position of the four boards in the Province. An overview of the financial position of these four boards for the three years ended 31 March 1999 is provided in Figure 1.

Figure 1 indicates that the financial position of the health and community services boards is deteriorating. As Figure 1 indicates the total liabilities of the four boards has increased from \$2.8 million in 1997 to \$3.8 million in 1998 and to \$10.5 million in 1999. In 1998-99, the Department provided an additional funding of \$2.3 million to these boards. If this \$2.3 million had not been provided, total liabilities of the boards would have increased from the \$10.5 million reported in Figure 1 to \$12.8 million.

Figure 1

#### Health and Community Services Boards Summary of Financial Position 31 March (\$Millions)

|                                   | 1999         |              |              |              |               | Total        |              |
|-----------------------------------|--------------|--------------|--------------|--------------|---------------|--------------|--------------|
|                                   | St. John's   | Eastern      | Central      | Western      | Total         | 1998         | 1997         |
| (Bank Indebtedness) Cash          | (1.8)        | (0.2)        | (0.6)        | 3.3          | <b>0.7</b>    | 9.0          | 3.9          |
| Accounts Payable                  | (2.1)        | (1.8)        | (0.8)        | (1.5)        | <b>(6.2)</b>  | (4.0)        | (3.3)        |
| Less: Accounts Receivable         | 3.4          | 1.4          | 1.4          | 0.8          | <b>7.0</b>    | 0.4          | 5.0          |
| <b>(Net Liability) Net Assets</b> | <b>(0.5)</b> | <b>(0.6)</b> | -            | <b>2.6</b>   | <b>1.5</b>    | <b>5.4</b>   | <b>5.6</b>   |
| Long-term Debt                    | (0.7)        | -            | -            | -            | <b>(0.7)</b>  | (0.9)        | (0.8)        |
| Severance Pay                     | (2.4)        | (1.2)        | (1.1)        | (1.1)        | <b>(5.8)</b>  | (3.7)        | (2.9)        |
| Vacation Pay                      | (0.9)        | (0.6)        | (0.5)        | (0.4)        | <b>(2.4)</b>  | (1.6)        | (1.4)        |
| Due to Board Fund                 | -            | -            | (0.7)        | (2.4)        | <b>(3.1)</b>  | (3.0)        | (3.3)        |
| <b>Total Liabilities</b>          | <b>(4.5)</b> | <b>(2.4)</b> | <b>(2.3)</b> | <b>(1.3)</b> | <b>(10.5)</b> | <b>(3.8)</b> | <b>(2.8)</b> |

Source: Audited Financial Statements

### 3.29 Health and Community Services Boards

#### Findings

As part of the on-going work of our Office, we review the financial statements and other information of the health and community services boards. Our review in 1999 included an assessment and comparison of the financial results and the financial position of the four boards in the Province. An overview of the financial position of these four boards for the three years ended 31 March 1999 is provided in Figure 1.

Figure 1 indicates that the financial position of the health and community services boards is deteriorating. As Figure 1 indicates the total liabilities of the four boards has increased from \$2.8 million in 1997 to \$3.8 million in 1998 and to \$10.5 million in 1999. In 1998-99, the Department provided an additional funding of \$2.3 million to these boards. If this \$2.3 million had not been provided, total liabilities of the boards would have increased from the \$10.5 million reported in Figure 1 to \$12.8 million.

Figure 1

#### Health and Community Services Boards Summary of Financial Position 31 March (\$Millions)

|                                   | 1999         |              |              |              |               | Total        |              |
|-----------------------------------|--------------|--------------|--------------|--------------|---------------|--------------|--------------|
|                                   | St. John's   | Eastern      | Central      | Western      | Total         | 1998         | 1997         |
| (Bank Indebtedness) Cash          | (1.8)        | (0.2)        | (0.6)        | 3.3          | <b>0.7</b>    | 9.0          | 3.9          |
| Accounts Payable                  | (2.1)        | (1.8)        | (0.8)        | (1.5)        | <b>(6.2)</b>  | (4.0)        | (3.3)        |
| Less: Accounts Receivable         | 3.4          | 1.4          | 1.4          | 0.8          | <b>7.0</b>    | 0.4          | 5.0          |
| <b>(Net Liability) Net Assets</b> | <b>(0.5)</b> | <b>(0.6)</b> | <b>-</b>     | <b>2.6</b>   | <b>1.5</b>    | <b>5.4</b>   | <b>5.6</b>   |
| Long-term Debt                    | (0.7)        | -            | -            | -            | <b>(0.7)</b>  | (0.9)        | (0.8)        |
| Severance Pay                     | (2.4)        | (1.2)        | (1.1)        | (1.1)        | <b>(5.8)</b>  | (3.7)        | (2.9)        |
| Vacation Pay                      | (0.9)        | (0.6)        | (0.5)        | (0.4)        | <b>(2.4)</b>  | (1.6)        | (1.4)        |
| Due to Board Fund                 | -            | -            | (0.7)        | (2.4)        | <b>(3.1)</b>  | (3.0)        | (3.3)        |
| <b>Total Liabilities</b>          | <b>(4.5)</b> | <b>(2.4)</b> | <b>(2.3)</b> | <b>(1.3)</b> | <b>(10.5)</b> | <b>(3.8)</b> | <b>(2.8)</b> |

Source: Audited Financial Statements

### 3.29 Health and Community Services Boards

In addition, we made the following observations regarding the financial position of the boards:

- Three of the four boards had bank overdrafts as of 31 March 1999 to finance a part of their operations. The four boards went from having cash of \$9.0 million in 1998 and \$3.9 million in 1997 to having a net cash position of only \$700,000 in 1999.
- Total net assets of \$1.5 million represents the amount by which the boards' current liabilities are exceeded by their liquid (cash convertible) assets. The boards went from having total net assets of \$5.4 million in 1998 to total net assets of \$1.5 million in 1999.
- After adding in long-term debt, severance pay, vacation pay and due to Board funds, Figure 1 shows that the total amount of funding required to meet the total liabilities of these four boards as at 31 March 1999 totalled \$10.5 million. The boards went from having total liabilities of \$3.8 million in 1998 to having total liabilities of \$10.5 million in 1999.

The \$10.5 million in total liabilities as at 31 March 1999 will be affected by the results of current operations and the level of funding by Government. If the boards have annual surpluses in the future, these surpluses could be used to fund their liabilities. If, on the other hand, the boards have annual deficits, these deficits, along with the liabilities, will also have to be funded.

Figure 2 shows the annual results of operations for the health and community services boards for the years ended 31 March 1997 to 31 March 1999. The figure indicates the deficits or surpluses before non-shareable expenses and after non-shareable expenses. The Department of Health and Community Services does not fund certain expenditures called non-shareable expenses. These non-shareable expenses do not require a cash outlay in that particular year and include depreciation, amortization, gain (loss) on disposal of capital assets, adjustments to incentives, net board operations and changes in severance pay and vacation pay accrual. These non-shareable expenses, however, may have to be funded sometime in the future.



### 3.29 Health and Community Services Boards

**Figure 2**

**Regional Health and Community Services Boards  
Summary of Annual Operating Results  
31 March  
(\$Millions)**

| Board                                                | Surplus (Deficit) before<br>Non-Shareable Expenses |            |            | Surplus (Deficit) after<br>Non-Shareable Expenses |            |            |
|------------------------------------------------------|----------------------------------------------------|------------|------------|---------------------------------------------------|------------|------------|
|                                                      | 1999                                               | 1998       | 1997       | 1999                                              | 1998       | 1997       |
| Health and Community Services - St. John's Region    | (3.2)                                              | .5         | 1.0        | (3.7)                                             | 0.1        | 0.7        |
| Eastern Health and Community Services Board          | (1.6)                                              | -          | 0.1        | (2.5)                                             | -          | (0.1)      |
| Central Regional Health and Community Services Board | (1.3)                                              | -          | 0.2        | (2.0)                                             | (0.2)      | -          |
| Western Regional Health and Community Services Board | (0.3)                                              | 1.7        | 2.2        | (0.5)                                             | 1.3        | 1.9        |
| <b>Sub-Total</b>                                     | <b>(6.4)</b>                                       | <b>2.2</b> | <b>3.5</b> | <b>(8.7)</b>                                      | <b>1.2</b> | <b>2.5</b> |
| Less: Additional funding provided                    | 2.3                                                | -          | -          | 2.3                                               | 0.0        | 0.0        |
| <b>Total</b>                                         | <b>(4.1)</b>                                       | <b>2.2</b> | <b>3.5</b> | <b>(6.4)</b>                                      | <b>1.2</b> | <b>2.5</b> |

Source: Audited Financial Statements and Department of Health and Community Services

Figure 2 indicates that all three boards which delivered the programs transferred from the Department of Human Resources and Employment (St. John's, Eastern and Central) incurred deficits after non-shareable expenses in 1999 ranging from \$2.0 million to \$3.7 million. Annual operating results for these three boards have deteriorated significantly since 1998 when only one of the boards, the Central Regional Health and Community Services Board incurred a deficit of \$200,000 after non-shareable expenses. Figure 2 also indicates that the Western Regional Health and Community Services Board reported a deficit of \$500,000 after non-shareable expenses in 1999 even though the community services programs were not transferred to it until the fiscal year 1999-2000.

During 1998-99, the Province provided the boards with additional funding of \$2.3 million. Without this funding the total deficits of the health and community services board would have increased from \$6.4 million to \$8.7 million.

### 3.29 Health and Community Services Boards

**Figure 2**

**Regional Health and Community Services Boards  
Summary of Annual Operating Results  
31 March  
(\$Millions)**

| Board                                                | Surplus (Deficit) before<br>Non-Shareable Expenses |            |            | Surplus (Deficit) after<br>Non-Shareable Expenses |            |            |
|------------------------------------------------------|----------------------------------------------------|------------|------------|---------------------------------------------------|------------|------------|
|                                                      | 1999                                               | 1998       | 1997       | 1999                                              | 1998       | 1997       |
| Health and Community Services - St. John's Region    | (3.2)                                              | .5         | 1.0        | (3.7)                                             | 0.1        | 0.7        |
| Eastern Health and Community Services Board          | (1.6)                                              | -          | 0.1        | (2.5)                                             | -          | (0.1)      |
| Central Regional Health and Community Services Board | (1.3)                                              | -          | 0.2        | (2.0)                                             | (0.2)      | -          |
| Western Regional Health and Community Services Board | (0.3)                                              | 1.7        | 2.2        | (0.5)                                             | 1.3        | 1.9        |
| <b>Sub-Total</b>                                     | <b>(6.4)</b>                                       | <b>2.2</b> | <b>3.5</b> | <b>(8.7)</b>                                      | <b>1.2</b> | <b>2.5</b> |
| Less: Additional funding provided                    | 2.3                                                | -          | -          | 2.3                                               | 0.0        | 0.0        |
| <b>Total</b>                                         | <b>(4.1)</b>                                       | <b>2.2</b> | <b>3.5</b> | <b>(6.4)</b>                                      | <b>1.2</b> | <b>2.5</b> |

Source: Audited Financial Statements and Department of Health and Community Services

Figure 2 indicates that all three boards which delivered the programs transferred from the Department of Human Resources and Employment (St. John's, Eastern and Central) incurred deficits after non-shareable expenses in 1999 ranging from \$2.0 million to \$3.7 million. Annual operating results for these three boards have deteriorated significantly since 1998 when only one of the boards, the Central Regional Health and Community Services Board incurred a deficit of \$200,000 after non-shareable expenses. Figure 2 also indicates that the Western Regional Health and Community Services Board reported a deficit of \$500,000 after non-shareable expenses in 1999 even though the community services programs were not transferred to it until the fiscal year 1999-2000.

During 1998-99, the Province provided the boards with additional funding of \$2.3 million. Without this funding the total deficits of the health and community services board would have increased from \$6.4 million to \$8.7 million.



### 3.29 Health and Community Services Boards

#### 1999-2000 Budgets

The operating deficits, before non-shareable expenses, projected for 1999-2000 by the health and community services boards are outlined in Figure 3.

As Figure 3 indicates, all boards are projecting significant deficits, before non-shareable expenses, totalling \$11.8 million for the 1999-2000 fiscal year. Included in the 1999-2000 base budgets for the health and community services boards is an additional \$4.0 million to help fund the deficits of the boards for 1999-2000. This additional funding of \$4.0 million decreases the projected deficits of \$11.8 million to a total projected deficit of \$7.8 million. We also note that although the boards have submitted their 1999-2000 budgets to the Department of Health and Community Services and were provided with tentative budget allocations in May of 1999, as of November 1999 (i.e. almost two thirds of this current fiscal year has passed), the final budgets have not yet been approved by the Department.

Figure 3

#### Health and Community Services Boards Actual and Projected Deficits Years ended 31 March (\$Millions)

| Board                                                | Actual Deficit<br>before Non-Shareable<br>Expenses | Projected Deficit<br>before Non-Shareable<br>Expenses |
|------------------------------------------------------|----------------------------------------------------|-------------------------------------------------------|
|                                                      | 1999                                               | 2000                                                  |
| Health and Community Services - St. John's Region    | (3.2)                                              | (5.0)                                                 |
| Eastern Health and Community Services Board          | (1.6)                                              | (2.3)                                                 |
| Central Regional Health and Community Services Board | (1.3)                                              | (2.7)                                                 |
| Western Regional Health and Community Services Board | (0.3)                                              | (1.8)                                                 |
| <b>Sub-Total</b>                                     | <b>(6.4)</b>                                       | <b>(11.8)</b>                                         |
| Less: Additional funding                             | 2.3                                                | 4.0                                                   |
| <b>Total</b>                                         | <b>(4.1)</b>                                       | <b>(7.8)</b>                                          |

Source: Audited financial statements and Department of Health and Community Services

### 3.29 Health and Community Services Boards

#### Department's Response

*The Department is aware of and concerned with the financial position of the Health and Community Services Boards. These Boards are currently going through a period of significant change as they integrate traditional community health programs with the programs transferred from the Department of Human Resources and Employment. The Department has reviewed the financial position of these Boards and will be taking a number of initiatives with the Boards to stabilize their financial position. With respect to the specific details of the report the following points should be noted:*

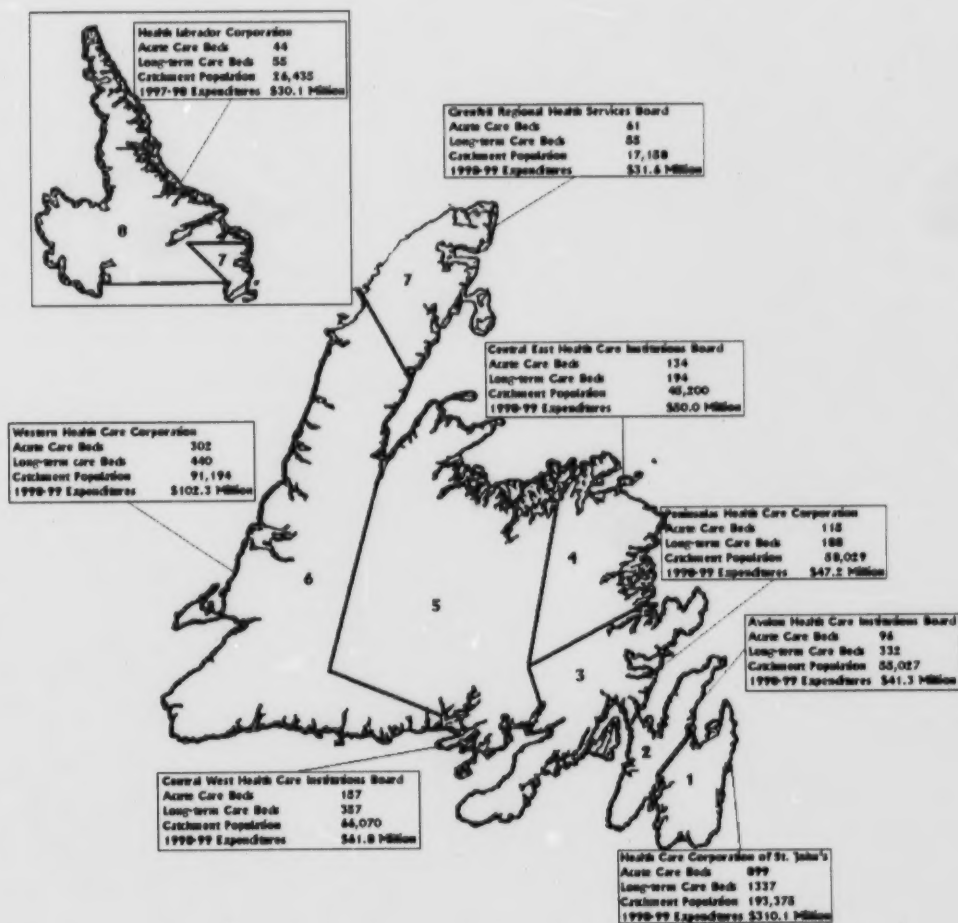
- *In reference to Figure 1, the long-term debt figure of \$0.7 million relates to long-term financing for the purchase of capital assets. The debt is being repaid on an annual basis through a fixed payment determination.*
- *In reference to Figure 1, severance and vacation pay, these two amounts of \$8.2 million represent an accrual of the vacation and severance liability recorded by the boards over the years, but does not require a cash outlay on an ongoing basis. An employee who leaves during a period is paid the amount of vacation and severance owed and the associated cash costs are paid and charged to current operations. The Department does not fund these total liabilities on a cash basis. The significant increase in these amounts is due to the additional staff taken over by the Health and Community Services Boards.*
- *In reference to Figure 2, with respect to the deficit of \$300,000 before non-shareable expenses incurred by the Western Health and Community Services Board in fiscal 1998-99, it should be noted this deficit arose due to the Department decreasing its funding contribution based on the Board forecasting a surplus budget position. The financial position of the Board subsequently changed which resulted in a small deficit being incurred.*

### 3.30 Monitoring Hospital Boards

From 1 November 1994 to 1 January 1996 the Government of Newfoundland and Labrador established eight regional health care institutions boards to administer health care facilities in Newfoundland and Labrador. These boards took over the facilities previously administered by many small local boards. Figure 1 shows these eight boards and the regions for which they are responsible.

Figure 1

#### Department of Health and Community Services Hospital Boards 31 March 1999





### 3.30 Monitoring Hospital Boards

In my 1998 Annual Report to The House of Assembly I reported on the financial condition of these hospital boards. This review indicated that as at 31 March 1998 the hospital boards had incurred \$32.3 million in bank debt and \$51.8 million in supplier debt to finance operating expenditures. This review also indicated that the boards would need \$62.7 million to pay their immediate financial commitments. During the 1998-99 fiscal year the Province provided these boards with an additional \$38.4 million to eliminate accumulated deficits to 31 March 1998. The actual payment of this money was not made until April 1999 and as a result the boards had bank indebtedness of \$39.1 million as at 31 March 1999. Figure 2 summarizes the financial position of the eight health care boards as at 31 March 1999 and 31 March 1998.

Figure 2

#### Hospital Boards Summary of Financial Position 31 March (\$ Millions)

|                                     | Board  |        |        |        |        |        |       |       | Total   |         |
|-------------------------------------|--------|--------|--------|--------|--------|--------|-------|-------|---------|---------|
|                                     | 1      | 2      | 3      | 4      | 5      | 6      | 7     | 8     | 1999    | 1998    |
| Cash on hand<br>(Bank Indebtedness) | (1.9)  | (5.0)  | (4.6)  | (2.6)  | (0.3)  | (22.5) | (1.3) | (0.9) | (39.1)  | (20.8)  |
| Accounts payable                    | (26.2) | (1.5)  | (4.5)  | (5.0)  | (4.9)  | (11.4) | (2.3) | (1.8) | (57.6)  | (48.9)  |
| Current LTD                         | (1.5)  | (0.3)  | (0.2)  | (0.4)  | (0.3)  | (0.1)  | (0.1) | -     | (2.9)   | (3.3)   |
| Less: Operating A/R                 | 22.8   | 1.9    | 4.5    | 1.4    | 0.9    | 9.2    | 1.6   | 1.4   | 43.7    | 23.1    |
| Net Liability                       | (6.8)  | (4.9)  | (4.8)  | (6.6)  | (4.6)  | (24.8) | 2.1   | (1.3) | (55.9)  | (49.9)  |
| Long-term debt                      | (1.2)  | (4.6)  | (6.2)  | (4.2)  | (5.6)  | (4.6)  | (2.9) | (1.3) | (30.6)  | (37.8)  |
| Severance pay                       | (36.3) | (4.6)  | (3.8)  | (5.1)  | (6.3)  | (12.7) | (3.0) | (1.9) | (73.7)  | (66.5)  |
| Vacation pay                        | (9.7)  | (1.5)  | (1.6)  | (2.2)  | (2.8)  | (2.9)  | (1.5) | (1.1) | (23.3)  | (22.4)  |
| Total debt before<br>funding        | (54.0) | (15.6) | (16.4) | (18.1) | (19.3) | (45.0) | (9.5) | (5.6) | (183.5) | (176.6) |
| Stabilization funding               | 1.0    | 0.5    | 1.0    | 0.5    | 0.3    | 5.5    | 0.2   | 1.0   | 10.0    | -       |
| One-time deficit<br>funding         | 10.2   | 2.2    | 3.9    | 2.4    | 1.8    | 15.4   | 0.8   | 1.7   | 38.4    | -       |
| Total unfunded<br>liabilities       | (42.8) | (12.9) | (11.5) | (15.2) | (17.2) | (24.1) | (8.5) | (2.9) | (135.1) | (176.6) |

Source: 31 March 1999 Audited Financial Statements except 31 March 1998 for #8, Health Labrador Corporation.  
Legend: See Figure 1

### 3.30 Monitoring Hospital Boards

In my 1998 Annual Report to The House of Assembly I reported on the financial condition of these hospital boards. This review indicated that as at 31 March 1998 the hospital boards had incurred \$32.3 million in bank debt and \$51.8 million in supplier debt to finance operating expenditures. This review also indicated that the boards would need \$62.7 million to pay their immediate financial commitments. During the 1998-99 fiscal year the Province provided these boards with an additional \$38.4 million to eliminate accumulated deficits to 31 March 1998. The actual payment of this money was not made until April 1999 and as a result the boards had bank indebtedness of \$39.1 million as at 31 March 1999. Figure 2 summarizes the financial position of the eight health care boards as at 31 March 1999 and 31 March 1998.

**Figure 2**

#### Hospital Boards Summary of Financial Position 31 March (\$ Millions)

|                                     | Board  |        |        |        |        |        |       |       | Total   |         |
|-------------------------------------|--------|--------|--------|--------|--------|--------|-------|-------|---------|---------|
|                                     | 1      | 2      | 3      | 4      | 5      | 6      | 7     | 8     | 1999    | 1998    |
| Cash on hand<br>(Bank Indebtedness) | (1.9)  | (5.0)  | (4.6)  | (2.6)  | (0.3)  | (22.5) | (1.3) | (0.9) | (39.1)  | (20.8)  |
| Accounts payable                    | (26.2) | (1.5)  | (4.5)  | (5.0)  | (4.9)  | (11.4) | (2.3) | (1.8) | (57.6)  | (48.9)  |
| Current LTD                         | (1.5)  | (0.3)  | (0.2)  | (0.4)  | (0.3)  | (0.1)  | (0.1) | -     | (2.9)   | (3.3)   |
| Less: Operating A/R                 | 22.8   | 1.9    | 4.5    | 1.4    | 0.9    | 9.2    | 1.6   | 1.4   | 43.7    | 23.1    |
| Net Liability                       | (6.8)  | (4.9)  | (4.8)  | (6.6)  | (4.6)  | (24.8) | (2.1) | (1.3) | (55.9)  | (49.9)  |
| Long-term debt                      | (1.2)  | (4.6)  | (6.2)  | (4.2)  | (5.6)  | (4.6)  | (2.9) | (1.3) | (30.6)  | (37.8)  |
| Severance pay                       | (36.3) | (4.6)  | (3.8)  | (5.1)  | (6.3)  | (12.7) | (3.0) | (1.9) | (73.7)  | (66.5)  |
| Vacation pay                        | (9.7)  | (1.5)  | (1.6)  | (2.2)  | (2.8)  | (2.9)  | (1.5) | (1.1) | (23.3)  | (22.4)  |
| Total debt before<br>funding        | (54.0) | (15.6) | (16.4) | (18.1) | (19.3) | (45.0) | (9.5) | (5.6) | (183.5) | (176.6) |
| Stabilization funding               | 1.0    | 0.5    | 1.0    | 0.5    | 0.3    | 5.5    | 0.2   | 1.0   | 10.0    | -       |
| One-time deficit<br>funding         | 10.2   | 2.2    | 3.9    | 2.4    | 1.8    | 15.4   | 0.8   | 1.7   | 38.4    | -       |
| Total unfunded<br>liabilities       | (42.8) | (12.9) | (11.5) | (15.2) | (17.2) | (24.1) | (8.5) | (2.9) | (135.1) | (176.6) |

Source: 31 March 1999 Audited Financial Statements except 31 March 1998 for #8, Health Labrador Corporation.  
Legend: See Figure 1



### 3.30 Monitoring Hospital Boards

Figure 2 indicates the following:

- As at 31 March 1999, all eight hospital boards had bank overdrafts totalling \$39.1 million and varied from \$300,000 for the Central West Health Care Institutions Board (Board #5) to \$22.5 million for the Western Health Care Corporation (Board #6).
- In April 1999 the Province provided the boards with \$38.4 million to eliminate deficits that existed as at 31 March 1998 and \$10 million for the 1998-99 deficits. This reduced the net liability to \$7.5 million which represented the amount by which the health care corporations' current liabilities exceeded their liquid assets.
- Although most of the operating debt of hospital boards has been eliminated there is still a significant unfunded liability. This includes \$30.6 million in long-term debt, \$73.7 million for severance pay due on retirement of employees and \$23.3 million in unused vacation pay.

The \$135.1 million in outstanding financial commitments of the health care corporations as at 31 March 1999 will be affected by the results of current operations and the injection of funds from Government. If the corporations have annual surpluses in the future, these surpluses could be used to fund their outstanding financial commitments. If, on the other hand, the corporations have annual deficits, these deficits will also have to be funded.

Figure 3 shows the annual results of operations for the health care corporations for the years ended 31 March 1998 and 31 March 1999. The figure indicates the deficits before non-shareable expenses and after non-shareable expenses. The Department of Health and Community Services does not fund certain expenditures called non-shareable expenses. These non-shareable expenses do not require a cash outlay in that particular year and include depreciation, amortization, gain (loss) on disposal of capital asset, adjustments to incentives, net board operations and changes in severance pay and vacation pay accrual. These non-shareable expenses, however, may have to be funded sometime in the future.

### 3.30 Monitoring Hospital Boards

**Figure 3**

**Hospital Boards  
Summary of Annual Operating Results  
1997-98, 1998-99  
(\$ Millions)**

|                                             | Deficit (Surplus) before<br>Non-Shareable Expenses |             | Deficit (Surplus) after<br>Non-Shareable Expenses |             |
|---------------------------------------------|----------------------------------------------------|-------------|---------------------------------------------------|-------------|
|                                             | 1998                                               | 1999        | 1998                                              | 1999        |
| Health Care Corporation of St. John's       | -                                                  | 4.3         | 5.0                                               | 9.0         |
| Avalon Health Care Institutions Board       | 1.1                                                | 1.1         | 1.6                                               | 1.7         |
| Peninsulas Health Care Corporation          | 1.4                                                | 1.0         | 2.3                                               | 1.8         |
| Central East Health Care Institutions Board | 1.1                                                | 1.4         | 2.1                                               | 2.0         |
| Central West Health Care Institutions Board | (0.6)                                              | (0.2)       | 2.0                                               | 0.7         |
| Western Health Care Corporation             | 4.4                                                | 3.1         | 7.0                                               | 4.9         |
| Grenfell Regional Health Services Board     | 0.6                                                | 1.3         | 0.7                                               | 2.0         |
| Health Labrador Corporation                 | 1.8                                                | 1.8         | 2.3                                               | 2.3         |
| <b>Total</b>                                | <b>9.8</b>                                         | <b>13.8</b> | <b>23.0</b>                                       | <b>24.4</b> |

Source: 31 March Audited Financial Statements except no audited financial statements have been received for Health Labrador Corporation for 31 March 1999 therefore 31 March 1998 amounts are used as an estimate for 1999.

As Figure 3 indicates all eight boards incurred deficits after non-shareable expenses in the 1998-99. Deficits ranged from approximately \$700,000 for Central West Health Care Institutions Board to \$9.0 million for Health Care Corporation of St. John's.

During 1998-99 the Province provided the boards with an additional \$10.0 million to help alleviate the 1998-99 deficits as there were significant deficits again in 1999. Despite the additional funding, the boards continue to incur significant operating deficits and only one board, Central West Institutions Board, was able to keep shareable expenditures within the available funding. In addition, our review indicated that all of the boards are projecting significant deficits in 1999-2000. Figure 4 indicates the actual deficit of each board for 1998-99 and the projected deficit for 1999-2000 before non-shareable expenses of depreciation, accrued severance pay and accrued vacation pay.

### 3.30 Monitoring Hospital Boards

**Figure 4**

**Hospital Boards  
Actual and Projected Deficits  
Years ended 31 March  
(\$ Millions)**

| Entity                                      | Actual Deficit (Surplus)<br>Before Non-shareable<br>Expenses | Projected Deficit<br>(Surplus) Before Non-<br>shareable Expenses |
|---------------------------------------------|--------------------------------------------------------------|------------------------------------------------------------------|
|                                             | 1999                                                         | 2000                                                             |
| Health Care Corporation of St. John's       | 4.3                                                          | 12.9                                                             |
| Avalon Health Care Institutions Board       | 1.1                                                          | 3.4                                                              |
| Peninsulas Health Care Corporation          | 1.0                                                          | 6.1                                                              |
| Central East Health Care Institutions Board | 1.4                                                          | 3.1                                                              |
| Central West Health Care Institutions Board | (0.2)                                                        | 3.8                                                              |
| Western Health Care Corporation             | 3.1                                                          | 15.7                                                             |
| Grenfell Regional Health Services Board     | 1.3                                                          | 1.3                                                              |
| Health Labrador Corporation                 | 1.8                                                          | 3.0                                                              |
|                                             | <b>13.8</b>                                                  | <b>49.3</b>                                                      |
| Less: Base budget increases                 | -                                                            | (17.4)                                                           |
| One time funding                            | -                                                            | (1.3)                                                            |
| <b>Total</b>                                | <b>13.8</b>                                                  | <b>30.6</b>                                                      |

Source: Department of Health and Community Services and audited financial statements

In October 1999 I requested a copy of the 1999-2000 budgets for the eight institutions boards. This information was provided by the Department of Health and Community Services and in addition I received a response from 1 of the 8 boards. This response indicated that the board had received a tentative allocation of funding but there has been no approval of the budgeted revenue and expenses by the Department of Health and Community Services.

### 3.30 Monitoring Hospital Boards

**Figure 3**

**Hospital Boards  
Summary of Annual Operating Results  
1997-98, 1998-99  
(\$ Millions)**

|                                             | Deficit (Surplus) before<br>Non-Shareable Expenses |             | Deficit (Surplus) after<br>Non-Shareable Expenses |             |
|---------------------------------------------|----------------------------------------------------|-------------|---------------------------------------------------|-------------|
|                                             | 1998                                               | 1999        | 1998                                              | 1999        |
| Health Care Corporation of St. John's       | -                                                  | 4.3         | 5.0                                               | 9.0         |
| Avalon Health Care Institutions Board       | 1.1                                                | 1.1         | 1.6                                               | 1.7         |
| Peninsulas Health Care Corporation          | 1.4                                                | 1.0         | 2.3                                               | 1.8         |
| Central East Health Care Institutions Board | 1.1                                                | 1.4         | 2.1                                               | 2.0         |
| Central West Health Care Institutions Board | (0.6)                                              | (0.2)       | 2.0                                               | 0.7         |
| Western Health Care Corporation             | 4.4                                                | 3.1         | 7.0                                               | 4.9         |
| Grenfell Regional Health Services Board     | 0.6                                                | 1.3         | 0.7                                               | 2.0         |
| Health Labrador Corporation                 | 1.8                                                | 1.8         | 2.3                                               | 2.3         |
| <b>Total</b>                                | <b>9.8</b>                                         | <b>13.8</b> | <b>23.0</b>                                       | <b>24.4</b> |

Source: 31 March Audited Financial Statements except no audited financial statements have been received for Health Labrador Corporation for 31 March 1999 therefore 31 March 1998 amounts are used as an estimate for 1999.

As Figure 3 indicates all eight boards incurred deficits after non-shareable expenses in the 1998-99. Deficits ranged from approximately \$700,000 for Central West Health Care Institutions Board to \$9.0 million for Health Care Corporation of St. John's.

During 1998-99 the Province provided the boards with an additional \$10.0 million to help alleviate the 1998-99 deficits as there were significant deficits again in 1999. Despite the additional funding, the boards continue to incur significant operating deficits and only one board, Central West Institutions Board, was able to keep shareable expenditures within the available funding. In addition, our review indicated that all of the boards are projecting significant deficits in 1999-2000. Figure 4 indicates the actual deficit of each board for 1998-99 and the projected deficit for 1999-2000 before non-shareable expenses of depreciation, accrued severance pay and accrued vacation pay.

### 3.30 Monitoring Hospital Boards

Figure 4

**Hospital Boards  
Actual and Projected Deficits  
Years ended 31 March  
(\$ Millions)**

| Entity                                      | Actual Deficit (Surplus)<br>Before Non-shareable<br>Expenses | Projected Deficit<br>(Surplus) Before Non-<br>shareable Expenses |
|---------------------------------------------|--------------------------------------------------------------|------------------------------------------------------------------|
|                                             | 1999                                                         | 2000                                                             |
| Health Care Corporation of St. John's       | 4.3                                                          | 12.9                                                             |
| Avalon Health Care Institutions Board       | 1.1                                                          | 3.4                                                              |
| Peninsulas Health Care Corporation          | 1.0                                                          | 6.1                                                              |
| Central East Health Care Institutions Board | 1.4                                                          | 3.1                                                              |
| Central West Health Care Institutions Board | (0.2)                                                        | 3.8                                                              |
| Western Health Care Corporation             | 3.1                                                          | 15.7                                                             |
| Grenfell Regional Health Services Board     | 1.3                                                          | 1.3                                                              |
| Health Labrador Corporation                 | 1.8                                                          | 3.0                                                              |
|                                             | <b>13.8</b>                                                  | <b>49.3</b>                                                      |
| Less: Base budget increases                 | -                                                            | (17.4)                                                           |
| One time funding                            | -                                                            | (1.3)                                                            |
| <b>Total</b>                                | <b>13.8</b>                                                  | <b>30.6</b>                                                      |

Source: Department of Health and Community Services and audited financial statements

In October 1999 I requested a copy of the 1999-2000 budgets for the eight institutions boards. This information was provided by the Department of Health and Community Services and in addition I received a response from 1 of the 8 boards. This response indicated that the board had received a tentative allocation of funding but there has been no approval of the budgeted revenue and expenses by the Department of Health and Community Services.

### **3.30 Monitoring Hospital Boards**

#### **Department's Response**

*The Department is aware of and concerned with the financial position of the regional hospital boards. The situation is not unique to this Province as most health facilities across the country are struggling with deficit problems. Government has made significant investments to support the operations of these boards and as you noted provided \$38.4 million to reduce the accumulated deficits at March 31, 1998. Provinces continue to request additional funding from the Federal Government through the CHST to support the publicly funded health system. The Department continues working with these boards to monitor their financial position and to achieve efficiencies.*

#### **Figure 2**

##### **Long-term Debt**

*The long-term debt figure of \$30.6 million relates primarily to financing for long-term care facilities operated by the regional hospital boards. Approximately \$24 million has been financed mostly through CMHC for these facilities where the financing has received a subsidy of either a reduced interest rate or a contribution by CMHC toward the interest costs. This debt is being repaid on an annual basis through a fixed payment determination.*

##### **Severance Pay/Vacation Pay**

*These two amounts of \$97.0 million represent an accrual of the vacation and severance liability recorded by the boards over the years, but does not require a cash outlay on an ongoing basis. An employee who leaves during a period is paid the amount of vacation and severance owed and the associated cash costs are paid and charged to current operations. The Department does not fund these total liabilities on a cash basis.*



### 3.31 Sale of Marystown Shipyard Facilities

#### Introduction

Prior to the sale of the shipyard operations, Marystown Shipyard Limited and Vinland Industries, [A Limited Partnership] operated facilities owned by Newfoundland Ocean Enterprises Limited (NOEL). All three companies are 100% owned by the Government of Newfoundland and Labrador.

Operations at Marystown were reported through Marystown Shipyard Limited, with fabrication operations being reported through Vinland Industries, [A Limited Partnership]. All significant capital assets at the facilities were owned directly by NOEL rather than by the operating entities.

Government's involvement with the Marystown shipyard facilities began in 1966 with the construction of the shipyard. The shipyard became operational in 1968, with the fabrication/offshore service facilities being added in 1993 at Cow Head. Both facilities are utilized for construction of new vessels. Shipyard operations include main hull assembly as well as repair and refit work. The fabrication/offshore service site is used for assembling deck houses and superstructures for new vessels as well as fabrication, repair and service work for offshore semi-submersible rigs, most notably relating to various projects connected with Hibernia development, including work related to the Gravity Base Structure, commonly referred to as the GBS.

In the fall of 1996, Government decided to divest itself of the facilities at Marystown and Cow Head. We were informed that a divestiture information package was prepared and distributed to several companies in the international steel fabrication sector. In June 1997, Friede Goldman International Inc. expressed interest in purchasing the facilities and on 24 September 1997, a Memorandum of Understanding was signed between Government and the company specifying the basic outline of an agreement by which the Province would sell the facilities.

On 22 December 1997, an Asset Purchase Agreement was signed between Government and a new company, Friede Goldman Marystown Ltd., later renamed Friede Goldman Newfoundland Ltd. (FGNL), transferring all of the facilities' assets to this company in exchange for 1,000 of its common shares. The net book value of the assets as disclosed in the audited interim financial statements of Newfoundland Ocean Enterprises Limited as at 31 December 1997 was \$61 million (\$86 million cost less accumulated depreciation of \$25 million).

On 1 January 1998, a Share Purchase Agreement was signed between Government, Friede Goldman Marystown Ltd., Friede Goldman Canada Inc., and Friede Goldman International Inc., to sell all shares of Friede Goldman Marystown Ltd. to Friede Goldman Canada Inc. for \$1.

### **3.31 Sale of Marystown Shipyard Facilities**

#### **Scope and Objectives**

Our objectives were to determine the extent of government's financial investment in the shipyard and to determine whether the provisions of the Asset Purchase Agreement and the Share Purchase Agreement are being complied with.

#### **Conclusions**

Based on historical information provided by the Department for 1966 through 1994 and through a review of the consolidated financial statements of Newfoundland Ocean Enterprises Limited for the years ended March 1995 through March 1999, government assistance to the Marystown shipyard facilities since 1966 totalled approximately \$115 million in capital and operating grants, and \$70.9 million in a loan guarantee which was assumed as direct debt of the Province in March 1999. As well, as part of the sales agreements, the Province maintained performance guarantees, which as at 31 March 1999 totalled approximately \$43 million. Friede Goldman Canada Inc. did indemnify Government relative to contracts it had assumed for which Government had performance guarantees in place. It also released Government relative to Government guarantees on contracts it had assumed between Marystown Shipyard Limited and an affiliated company.

Not all the conditions included in the sales agreements have been met. In particular, reports relating to man hours of work for the calendar year 1998 and net after tax profits for the 12 months ending March 1998 were not submitted in accordance with agreement provisions. The report relating to man hours of work for 1998, due to be submitted by 28 February 1999, was never submitted although a Cabinet Committee was provided with this information verbally by company officials in March 1999. The report to indicate the net after tax profits, due to be submitted by 30 June 1998, was not submitted until May 1999.

The Share Purchase Agreement does not require that information provided by Friede Goldman Newfoundland Limited on man hours be audited or otherwise independently verified. The Agreement does provide that the company must retain related information and that Government and its representatives shall have access to such information upon reasonable request and on reasonable notice. Discussions with the Department indicated that the unaudited information provided by the company for 1998 was never verified by Government.

The sales agreements do not require Friede Goldman Newfoundland Limited to meet any employment or other requirements after the term of the agreements has passed, which is 31 December 2000. As well, there is no provision for assets, recorded at a cost of approximately \$86 million at the time the agreements were signed, to return to the Province in the event the company does not comply with the agreements or if the company decided to divest itself of the facilities. In minutes of a Newfoundland

### 3.31 Sale of Marystown Shipyard Facilities

Ocean Enterprises Limited/Marystown Shipyard Limited Board meeting held 5 September 1997, it was noted with respect to a discussion held with the Cabinet Committee established to oversee the divestiture, that *"The Cabinet Committee wants the terms of guaranteed employment extended beyond 3 years and wants to incorporate language covering the return of the assets to the Province in the event of certain occurrences."* This was never included in any of the Agreements.

A divestiture information package was prepared and distributed to several companies in the international steel fabrication sector. While the Department did provide a copy of the divestiture information provided to the potential proponents, we were advised that no formal record existed as to whom the divestiture information was provided and the evaluation process followed for any proposals which may have been received.

#### Detailed Findings Financial Information

Figure 1 provides an overview of consolidated financial information for Newfoundland Ocean Enterprises Limited for the four years ending prior to the shipyard sale, from March 1994 through March 1997, and for the most recent two year ends subsequent to the sale.

As indicated in Figure 1, the company reported significant losses for each of the years ended March 1994 through March 1998.

Figure 1

#### Consolidated Financial Information Newfoundland Ocean Enterprises Limited Years Ended March (\$000)

| Year | Total Assets | Total Liabilities | Deferred Government Assistance | Total Equity (Deficiency) | Total Revenue | Total Expenses | Other Losses | Net Loss    |
|------|--------------|-------------------|--------------------------------|---------------------------|---------------|----------------|--------------|-------------|
| 1994 | \$ 79,777    | \$ 41,821         | \$ 50,661                      | \$ (12,705)               | \$ 33,831     | \$ 48,445      | \$ (1,362)   | \$ (15,976) |
| 1995 | 96,383       | 76,203            | 49,405                         | (29,225)                  | 73,387        | 89,907         | 0            | (16,520)    |
| 1996 | 70,225       | 63,413            | 46,552                         | (39,740)                  | 42,799        | 53,314         | 0            | (10,515)    |
| 1997 | 73,744       | 75,663            | 43,191                         | (45,110)                  | 21,083        | 26,453         | 0            | (5,370)     |
| 1998 | 1,381        | 72,024            | 0                              | (70,643)                  | 66,260        | 69,268         | (22,525)     | (25,533)    |
| 1999 | 359          | 340               | 0                              | 19                        | 13            | 251            | 0            | (238)       |

Source: Audited financial statements

Note: The other losses classification in 1998 relates to losses on sale of the Marystown facilities as disclosed in the audited financial statements

### 3.31 Sale of Marystown Shipyard Facilities

#### Government Assistance

Government has provided considerable assistance to the Marystown facilities. This assistance took the form of capital and operations grants totaling \$115 million and the assumption of the company's long-term debt of \$70.9 million in March 1999.

As indicated in Figure 2, Government provided guarantees to applicable banks as security to finance losses and working capital deficiencies through bank indebtedness and long-term debt and performance guarantees for major capital contracts. Figure 2 provides an overview of the history of these guarantees since 1992, as disclosed in the Public Accounts of the Province.

**Figure 2**

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**Government Guarantees  
Newfoundland Ocean Enterprises Limited  
Years Ended 31 March  
(\$ Millions)**

| Approval Date | Corporate Guarantee | Performance Guarantee |
|---------------|---------------------|-----------------------|
| 1992          | \$ 16.70            | \$ 0.00               |
| 1993          | 17.40               | 0.00                  |
| 1994          | 50.10               | 0.00                  |
| 1995          | 79.20               | 0.00                  |
| 1996          | 55.60               | 7.80                  |
| 1997          | 67.80               | 52.50                 |
| 1998          | 70.00               | 70.20                 |
| 1999          | 0.00                | 42.80                 |

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Source: Public Accounts of the Province

### 3.31 Sale of Marystown Shipyard Facilities

Figure 3 provides an overview of assistance provided by Government as reflected in historical information provided by the Department for 1966 through 1994, and the audited consolidated financial statements of Newfoundland Ocean Enterprises Limited for the three years ending prior to the shipyard sale and for the two years ended since the sale.

During the year ended March 1999, Government assumed NOEL's debt, in the amount of \$70.9 million, which had been secured by a Government guarantee.

#### Divestiture

In January 1997, Cabinet authorized the Minister of Industry, Trade and Technology to provide a clear mandate to the Board of Directors of the Marystown Shipyard Limited to pursue the divestiture of that Crown corporation under general direction from Government. The direction was to include:

- forming an ad hoc committee of Ministers, with whom the Board could confer with and seek policy direction from;

Figure 3

**Government Assistance  
Newfoundland Ocean Enterprises Limited  
Years Ended March  
(\$Millions)**

| Year                | Capital Grants Received | Operations Grants Received | Bank Indebtedness Guarantee | Long Term Debt Guarantee | Assumption of Bank Debt |
|---------------------|-------------------------|----------------------------|-----------------------------|--------------------------|-------------------------|
| 1966 - 1994         | 43.40                   | 56.40                      | 28.30                       | 0.00                     | 0.00                    |
| 1995                | 1.70                    | 2.20                       | 38.40                       | 1.20                     | 0.00                    |
| 1996                | 0.40                    | 3.80                       | 56.40                       | 0.60                     | 0.00                    |
| 1997                | 0.00                    | 3.50                       | 67.30                       | 0.00                     | 0.00                    |
| 1998                | 0.00                    | 3.60                       | 69.60                       | 0.00                     | 0.00                    |
| 1999                | 0.00                    | 0.00                       | 0.00                        | 0.00                     | 70.90                   |
| <b>Total Grants</b> | <b>45.50</b>            | <b>69.50</b>               | <b>N/A</b>                  | <b>N/A</b>               | <b>70.90</b>            |

Source: Government's records and Audited financial statements of NOEL



### 3.31 Sale of Marystown Shipyard Facilities

- targeted investors to be limited to national and international companies with the financial capability and market access in appropriate sectors to operate the shipyard as a going concern, with prolonged discussions to be limited to proponents prepared to put forward a detailed business plan for operation of the yard in the long term;
- a purchase price in the order of \$25 million to be used as a starting point for discussion with potential buyers;
- proposals involving the purchase of either of the shipyard or the Cow Head facilities to be given due consideration;
- designation under the Province's EDGE legislation to be seriously considered for activities not deemed to have a competitive impact on other Newfoundland entities;
- new owners shall be exempt from any environmental liability associated with the current operation;
- if required, a commitment shall be given to potential new owners that no financial assistance will be provided by the Province toward the establishment, acquisition, or expansion of substantial competing facilities;
- additional costs associated with travel, professional fees and other expenses associated with the divestiture effort, up to a total of \$250,000 shall be approved on a case by case basis, with the yard's line of credit and the corresponding loan guarantee from the Province to be increased to accommodate these additional costs as necessary;
- final decisions with respect to divestiture to be made by Cabinet; and
- an appropriate communications strategy relating to divestiture to be developed.

Government struck a committee, comprising the Premier, the Minister of Finance and President of Treasury Board, and the Ministers of Mines and Energy, Industry, Trade and Technology, and Works, Services and Transportation, to negotiate all issues with respect to the divestiture of the shipyard facilities, including the completion of a divestiture agreement.



### 3.31 Sale of Marystown Shipyard Facilities

There was no determination of the value of the assets that would be sold in the event that the divestiture proceeded.

A divestiture information package was prepared and distributed to several companies in the international steel fabrication sector. While the Department did provide a copy of the divestiture information provided to the potential proponents, we were advised that no formal record existed of to whom the divestiture information was provided and the evaluation process followed for any proposals which may have been received.

We were informed that in June 1997, Friede Goldman International Inc. (FGI) expressed interest in purchasing the facilities. On 24 September 1997, a Memorandum of Understanding was signed between Government and FGI, specifying the basic outline of an agreement by which the Province would sell the facilities.

Under the Memorandum, Government agreed to:

- incorporate a new company to which assets and uncompleted contracts would be transferred, in exchange for all issued and outstanding shares of the new company. All shares of the new company were then to be transferred to Friede Goldman International Inc. or its subsidiary;
- provide EDGE status for the new company;
- consult with the chief executive officer of the new company regarding the impact of any future Government investment in competing operations; and
- maintain certain performance guarantees for ongoing contracts.

In exchange, Friede Goldman International Inc. agreed to:

- maintain a minimum of 1.2 million man hours per year for the calendar years 1998, 1999 and 2000 and in default be required to pay Government \$10 million, \$5 million and \$5 million respectively;
- pay 50% of any net after tax profit of the facilities to Government relating to the year ended March 1998;

### 3.31 Sale of Marystown Shipyard Facilities

- complete specified upgrades and repairs and invest an intended \$5 million to \$15 million in capital improvements; and
- provide Government with at least 90 days notice of any intended cessation of operations.

On 22 December 1997, an Asset Purchase Agreement was signed between Government and Friede Goldman Marystown Ltd., later renamed Friede Goldman Newfoundland Ltd. (FGNL), transferring all of the facilities' assets to FGNL in exchange for 1,000 of its common shares. FGNL is the new company envisaged in the Memorandum of Understanding. Included in the Agreement is a provision for working capital being available to FGNL at closing of at least \$2.5 million. As soon as practicable after closing date, FGNL was to arrange for the completion of an audit, for the purpose of determining the accuracy of the calculation of the \$2.5 million adjusted working capital required to be transferred to FGNL on closing. Any difference was to be paid or recovered by the applicable party with provision made for resolution of any dispute through arbitration. The Agreement contained provisions as outlined in the Memorandum of Understanding with respect to Government providing EDGE status and consulting with the chief executive officer of FGNL regarding the impact of any future Government investment in competing operations.

On 1 January 1998, a Share Purchase Agreement was signed between Government, FGNL, Friede Goldman Canada Inc. (FGCI), and FGI, to sell all shares of FGNL to Friede Goldman Canada Inc. for \$1. The Agreement contained the same provisions outlined under the Memorandum of Understanding with respect to minimum man hour requirements, payment of net after tax profit of the facilities relating to the year ended March 1998, completion of specified upgrades and repairs and investment in capital improvements, and provision to Government of at least 90 days notice of any intended cessation of operations. With respect to performance guarantees by Government on ongoing projects, the Memorandum of Understanding provided for the maintenance of performance guarantees with the exception of guarantees for projects with FGI affiliated companies. The Share Purchase Agreement provides that FGCI would indemnify Government with respect to all ongoing projects with the exception of one with an affiliated company, Government's guarantee for which would be released.

The Share Purchase Agreement also provides time frames for the completion of various provision requirements. Within 90 days subsequent to 31 March 1998, FGNL was to deliver to Government an audited statement setting out the calculated net after tax profit, with any related payment to be made by no later than 31 May 1998. As well, within 60 days subsequent to each calendar year end for 1998, 1999, and 2000, FGNL is

### **3.31 Sale of Marystown Shipyard Facilities**

to report to Government the actual man hours relating to the preceding year, with any default amount payable to be included with the statement.

Under the Share Purchase Agreement, FGI guarantees the performance and related payments of all commitments made by FGCI and FGNL, including the payment of any out-of-pocket costs and expenses reasonably incurred by Government or NOEL and MSL in connection with enforcing commitments made by FGCI and FGNL.

Subsequent to divestiture, Vinland Industries, [A Limited Partnership] became essentially inactive with consideration currently being given by Government to having the Corporation dissolved. NOEL and MSL will continue to exist, primarily to facilitate any legal or other issues which may arise with respect to the divestiture.

#### **Compliance with Agreements**

Our review of the requirements set out in the Asset Purchase Agreement and a review of events subsequent to the date of the Agreement disclosed the following:

- In May 1997, Cabinet had authorized the designation of Marystown Shipyard Limited as an EDGE corporation for the purpose of facilitating its sale to the private sector. Cabinet authorized the designation of FGNL as an EDGE corporation in September 1997.
- As soon as practicable after 31 December 1997, FGNL was to have an audit conducted for the purposes of determining the accuracy of the calculation of the \$2.5 million adjusted working capital required by FGNL on 31 December 1997. Upon completion of the audit, should it be determined that the amount of working capital required was other than \$2.5 million, Government was to pay to FGNL any shortfall, and FGNL was to pay to Government any excess. Payments were to be made within 30 days after the audit was completed, with a further stipulation that in the event of a dispute, the payment would not be required until 15 days after a decision by an arbitrator.

In May 1998, the auditors for FGNL reported that the working capital shortfall was \$3.809 million, less an advance payment by Government of \$905,000, for a net amount due to FGNL of \$2.904 million. In the report, the auditors outlined that this amount may be adjusted to \$1.534 million depending on the interpretation of whether a long term holdback receivable amount would be included in the working capital calculation.

### 3.31 Sale of Marystown Shipyard Facilities

In a separate report in August 1998, a private sector auditor engaged by the Department, determined that the working capital shortfall was only \$1.973 million, less the \$905,000 advance, for a net of \$1.068 million. After additional review, the Department's auditor revised the original estimate of \$1.068 million to a range of between \$1.250 million and \$1.300 million. The revision was based mainly on an estimate of the overhead contribution for a major contract. The final settlement amount of \$1.260 million was paid in September 1998.

Our review of the requirements set out in the Share Purchase Agreement and a review of events subsequent to the date of the Agreement disclosed the following:

- FGCI did indemnify Government relative to contracts it had assumed for which Government had performance guarantees in place. It also released Government relative to Government guarantees on contracts it had assumed between Marystown Shipyard Limited and an affiliated company. These actions were agreed to through a schedule appended to the Share Purchase Agreement.
- FGNL was to submit a report, in writing, to Government within 60 days after each calendar year end for 1998, 1999, and 2000, setting out the actual man hours utilized for the immediately preceding calendar year. FGNL did not submit a formal report as required under the Agreement. It did, however, in a March 1999 presentation to the Economic Advisory Committee of Cabinet, report that it had maintained the required 1.2 million man hours, consisting of management and labour, and salaried and hourly, for the calendar year 1998. Actual hours reported were 1.7 million. It appears uncertain whether the 1.2 million man hour requirement will be met for the calendar year 1999. FGNL has advised Government that man hours for the six month period ended 30 June 1999 were approximately 459,000. It is noted that if FGNL is found to be in default of this requirement for 1999, damages in the amount of \$5 million will be required to be paid by FGNL to Government.

The Agreement does not require that the report on man hours from FGNL be audited or otherwise independently verified. The Agreement does provide that FGNL must retain related information and that Government and its representatives shall have access to such information upon reasonable request and on reasonable notice. Discussions with the Department indicated that the information presented by FGNL was not verified by Government.

### 3.31 Sale of Marystown Shipyard Facilities

- We were advised that through discussion with FGNL and through its own knowledge of the facilities' operations, Government determined that FGNL had upgraded the existing computer system, repaired the synchro-lift and provided other equipment within three months after the Agreement date. As well, in the March 1999 presentation to the Economic Advisory Committee of Cabinet, FGNL reported that it had invested in excess of \$8 million in capital improvements, which was within the required investment of between \$5 million and \$15 million in capital improvements outlined in the Share Purchase Agreement. No further verification was carried out on the reported \$8 million in capital improvements.
- FGNL was to submit a statement to Government within 90 days after 31 March 1998, signed and verified by FGNL and audited by FGNL's auditors, setting out the calculated net after tax profit of FGNL for the 12 months ending March 1998. FGNL did not meet the required timeframe. The audited statement setting out the calculated net after tax profit was not submitted until May 1999. In the statement, it was reported that the net after tax loss was \$1,885,400. Under the Agreement, FGNL was to pay Government 50% of any calculated net after tax profit, therefore, there was no payment to be made.

#### Department's Response

*Over the years, as detailed in your report, government provided considerable financial support to Marystown Shipyard. Prior to its sale, the Board of Directors implemented a number of strategies to turn the facility around and make it attractive to the private sector since it was a widely held view that the Shipyard could be operated more efficiently and effectively in private hands. The sale to Friede Goldman, then, was the culmination of these efforts.*

*With respect to your comments on proposals from other interested parties, I want to make it clear that the offer from Friede Goldman was the only real expression of interest that we had in the facility. There were preliminary discussions with a major Canadian shipping company, however, there was no proposal or exchange of correspondence. In short, the Friede Goldman offer was the full extent of the private sector interest in the purchase of Marystown Shipyard.*



### 3.32 Newfoundland Government Fund Limited

#### Introduction

The Newfoundland Government Fund Limited was incorporated on 10 November 1995 under the *Corporations Act* of the Province of Newfoundland. All shares of the Corporation are held by Ministers of the Crown on behalf of the Province. Its affairs are governed by a Board of Directors which is elected by the shareholders of the Corporation.

The Corporation is a Government-administered venture capital fund under the *Immigration Act* (Canada) and Regulations. Under the Canadian Immigrant Investor Program, the Corporation issued an Offering Memorandum in September of 1996 to raise funds from immigrant investors in order to provide loan and equity capital to establish, expand, purchase, maintain or revitalize businesses or commercial ventures in Newfoundland. For the immigrant investors, in addition to earning a nominal return on their capital, their investment in the Corporation helps satisfy a portion of their visa requirements under Canada's Immigrant Investor Program.

The offering was comprised of units each of which represents a \$250,000 promissory note bearing interest at the simple rate of 2% per annum. Although the promissory note is repayable in full five years from the date on which 70% of the investor proceeds are invested or upon refusal of an investor's Canadian visa application, neither the Government of Canada nor the Government of the Province of Newfoundland offers any guarantees or assurances of a return on an investor's original investment and neither government is liable for any loss or damages that may be suffered by an investor as a result of the investment in the securities. The minimum and maximum amounts of the offering were \$3,500,000 (14 units) and \$35,000,000 (140 units) respectively.

For the purposes of facilitating the marketing and closing of these investment units, the Corporation engaged the services of an escrow and distribution agent. For the provision of these services, as at 31 December 1998, the Corporation incurred distribution and marketing fees of \$875,000 (7% of the offering proceeds of \$12,500,000) and reporting and liaison fees of \$87,994 (0.6% annually of the offering proceeds).

The offering expired on 30 June 1998. As of 30 April 1999, Citizenship and Immigration Canada required the Corporation to finalize its investor listing to the maximum offering of 140 units. Figure 1 provides information on the status of these 140 investor units at 30 September 1999.



### 3.32 Newfoundland Government Fund Limited

**Figure 1**

**Status of Investor Units  
30 September 1999**

| Status of Investor Units                                                                                  | # of Units | Proceeds Held by Fund | Unit Deposits Held By Escrow Agent | Subscription Proceeds Receivable | * Total Potential Subscription Proceeds |
|-----------------------------------------------------------------------------------------------------------|------------|-----------------------|------------------------------------|----------------------------------|-----------------------------------------|
| Units Closed                                                                                              | 54         | \$13,500,000          | \$ -                               | \$ -                             | \$13,500,000                            |
| Units with full subscription proceeds; awaiting approval of Fund for closure and release proceeds to Fund | 28         | -                     | 7,000,000                          | -                                | 7,000,000                               |
| Units for which the full subscription proceeds have not been received                                     | 56         | -                     | 1,105,648                          | 12,894,352                       | 14,000,000                              |
| Units Refunded to Investors                                                                               | 2          | -                     | -                                  | -                                | -                                       |
| <b>Total</b>                                                                                              | <b>140</b> | <b>\$13,500,000</b>   | <b>\$8,105,648</b>                 | <b>\$12,894,352</b>              | <b>\$34,500,000</b>                     |

Source: HSBC Capital - Final list of subscribers

\* This assumes the remaining 138 units will be closed.

Effective 1 April 1999, Citizenship and Immigration Canada announced the implementation of the new Immigrant Investor Program and Regulations to govern this program. The new program was designed to increase economic benefits to Canada and the provinces, further reduce the potential for abuse and reduce the level of resources required of governments to administer the program.

In accordance with the new regulations, the Federal government will act as an agent on behalf of the provinces and territories, which will determine where to invest the money. The immigrant investment under the new program will now be secured by the provinces and territories against loss. Regulations governing the current program are repealed, but will continue to apply to previously approved funds. Thus, with the exception of Quebec, provinces can no longer operate their own immigrant investor programs unless these programs existed before the new Regulations came into effect on 1 April 1999.



### 3.32 Newfoundland Government Fund Limited

Figure 1

#### Status of Investor Units 30 September 1999

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| Units for which the full subscription proceeds have not been received                                     | 56         | -                     | 1,105,648                          | 12,894,352                       | 14,000,000                              |
| Units Refunded to Investors                                                                               | 2          | -                     | -                                  | -                                | -                                       |
| <b>Total</b>                                                                                              | <b>140</b> | <b>\$13,500,000</b>   | <b>\$8,105,648</b>                 | <b>\$12,894,352</b>              | <b>\$34,500,000</b>                     |

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### 3.32 Newfoundland Government Fund Limited

In 1998, we performed a review of the Newfoundland Government Fund Limited. In our 1998 Annual Report to the House of Assembly we concluded that:

- The Corporation was not in compliance with Canadian Immigration Regulations as it had not met required deadlines for investing a minimum of 70% of the investment proceeds (\$4,025,000 up to 30 September 1998) in eligible business operations within 9 months of receiving the proceeds. In addition, the Corporation did not provide annual audited financial statements to Citizenship and Immigration Canada by the required deadline.
- The Corporation was not in compliance with all of the terms of the Offering Memorandum as it had not maintained the required 20% of the subscription proceeds (\$1,250,000 up to 30 September 1998) in a repayment account for investment in Canadian liquid securities. This repayment account is for the purpose of refunding those investors whose visa applications are rejected. In addition, unaudited interim financial statements of the Fund were not distributed to investors as required by the Offering Memorandum and the annual audited financial statements were not distributed to investors until after the deadline established in the Offering.
- The Fund had not exercised all of its rights as permitted under the Offering Memorandum. One such right includes the ability to have the Escrow agent enforce the requirement that investors make the minimum required deposit and pay the balance within the required time frame. In addition, although permitted under the Offering, the Corporation had not requested any support for marketing fees charged to the Fund by the Distribution agent (\$117,500 up to 30 September 1998).
- The Corporation had not developed any policies regarding the selection, monitoring and evaluation of consultants. In addition, the Corporation could not provide information on how the various consultants were selected.
- The Corporation's records were not properly maintained, resulting in the Corporation not being able to locate various documents or only locating certain documents after much effort.

### 3.32 Newfoundland Government Fund Limited

#### Scope and Objectives

We updated our review of Newfoundland Government Fund Limited in October 1999. The objectives of our review were to determine the status of the investment units and to assess the Corporation's progress with respect to our observations and recommendations included in our 1998 report.

#### Conclusions

Although the Corporation has raised \$13.5 million under the Canadian Immigrant Investor Program to provide capital to businesses and commercial ventures in Newfoundland which meet the requirements of the Program, the Corporation has been unsuccessful in investing any of the funds as of October 1999. As a result, the Corporation has not complied with the *Immigration Act* (Canada) and Regulations. For example:

- The Corporation has not invested any of the required 70% of the \$13.5 million investment proceeds (or \$9.45 million) in eligible business operations within 9 months after the release of the proceeds from the escrow agent; and
- The Corporation has not submitted its annual audited financial statements for the year ended 31 December 1998 to Citizenship and Immigration Canada as of October 1999 although they were required to be submitted by 20 May 1999.

In addition, the Corporation has not complied with the Confidential Offering Memorandum. For example:

- The Corporation has never distributed unaudited interim financial statements to investors by 28 September of each year;
- The Corporation did not submit the annual audited financial statements to the escrow agent in time for distribution to the investors by 30 April of each year;
- The Corporation has not maintained the required 20% of the subscription proceeds (\$2,700,000 up to 30 September 1999) in a repayment account for investment in Canadian liquid securities. At 30 September 1999, the balance in the Corporation's repayment account was \$1,651,088; and
- The Fund had still not exercised its rights as permitted under the Offering Memorandum to have the Escrow agent enforce the requirement that investors make the minimum required deposit and pay the balance within the required time frame.

### **3.32 Newfoundland Government Fund Limited**

Since our last review, an additional \$548,374 in consulting and professional fees have been paid by the Corporation. However, almost all of these fees were paid for the continuing services of consultants selected in previous years, including fees to the Escrow and Distribution agent of \$508,106. No additional consulting contracts have been entered into by the Corporation since we raised this concern in last years report.

#### **Findings and Recommendations**

#### **Compliance with Canadian Immigration Regulations**

As an approved Government-administered venture capital fund, the Corporation is required to comply with the Canadian Immigration Regulations under the *Immigration Act* (Canada). In accordance with the Regulations, the Minister of Citizenship and Immigration Canada may suspend the approval of the Newfoundland Government Fund Limited if the Corporation does not comply with certain terms or conditions. Our review indicated the following instances of non-compliance:

##### **1. Investment of Subscription Proceeds**

The Regulations require that the Corporation invest at least 70% of the investment proceeds in eligible business operations within 9 months after the release of the proceeds from the escrow agent. As at 30 September 1999, \$13,500,000 in subscription proceeds, representing 54 units, had been received by the Corporation between the period of 13 June 1997 and 7 January 1999. Under the Regulations, \$9,450,000 (70%) of this amount was required to have been invested in eligible projects within 9 months of receiving these funds; however, none of these funds have been invested. As a result, the Corporation is not in compliance with Canadian Immigration Regulations.

In 1998, the Corporation approved the use of investor funds for the construction of the Harbour Breton hospital. From the period June 1998 to January 1999, the Corporation advanced \$1,570,000 to a trust account established for use in paying for the construction of this hospital facility. Officials indicated that the project was subsequently canceled and as a result, in early 1999 the Province assumed direct responsibility for this capital project and refunded the \$1,570,000 to the Corporation.



### **3.32 Newfoundland Government Fund Limited**

Since the project was canceled, the Corporation was in a state of regulatory "non-compliance" with the *Immigration Act* (Canada) and Regulations as funds received as early as 13 June 1997 should have been invested within 9 months or 13 March 1998. Investors began to express concern as their proceeds had still not been invested by the Corporation. To compensate investors for delays in investing in eligible projects, the Board of Directors of the Corporation approved an increase in the interest rate paid to investors from 2% to 5%. This policy applies only to the 54 investors whose proceeds have been held by the Corporation for more than 9 months and is not in effect until 5 years and 9 months from the respective closing dates of their units. For example, for the investor whose unit closed on 13 June 1997, the interest rate would increase to 5% on 13 March 2002.

At the end of our review in October 1999, three investments in eligible projects have been identified and approved by the Corporation's Board of Directors and Treasury Board. These projects involve providing funding for the construction of three health care facilities to be located in Fogo Island, Bonne Bay and Grand Bank. Citizenship and Immigration Canada approved the investments for health care facilities in Fogo and Bonne Bay on 29 September 1999; however, approval for the Grand Bank project is still pending. The prime consultants for each project have been selected but as of 14 October 1999, contracts between these consultants, the Department of Works, Services and Transportation, the applicable health care board and the Corporation have not been signed. Consequently, no funds have been transferred from the Corporation nor have tenders been called for the selection of the developer for each of the projects.

#### **2. Audited Financial Statements**

The Regulations require that the Corporation provide annual audited financial statements to Citizenship and Immigration Canada within 140 days after the end of each financial year i.e. 20 May. The Corporation's financial statements for the year ended 31 December 1996 and 1997 were not submitted to the Federal department until June 1998. Financial statements for the year ended 31 December 1998 have not been submitted to Citizenship and Immigration Canada as of October 1999.

#### **Compliance with the Confidential Offering Memorandum**

The Corporation issued a Confidential Offering Memorandum in September 1996 which outlined the terms and conditions of investment to potential investors. The Corporation is not in compliance with all of the terms of the Confidential Offering Memorandum, nor has it exercised all of its rights in accordance with the Memorandum. For example:

### 3.32 Newfoundland Government Fund Limited

- To enable the Corporation to refund those unit holders whose visa applications are rejected, the Corporation is required to establish a repayment account and deposit 20% of the subscription proceeds in the account for investment in Canadian liquid securities. At 30 September 1999, the balance in the Corporation's repayment account was \$1,651,088; however, in accordance with the 20% requirement, the balance should have been \$2,700,000. The Corporation has recently taken steps to ensure that the required balance is maintained in the repayment account for any new units being closed by the Corporation; however, adjustments will have to be made for units closed prior to January 1999 in order to meet the required balance of \$2,700,000.
- The escrow agent is required to distribute annual audited financial statements to investors within 120 days of 31 December i.e. 30 April. The Corporation did not provide the financial statements for the year ended 31 December 1998 to the escrow agent until June 1999. The escrow agent subsequently distributed the financial statements to investors in July 1999. In addition, the Offering Memorandum requires that unaudited interim financial statements for 30 June be distributed to investors within 90 days i.e. 28 September. Such statements have never been issued.
- Under the terms of the Confidential Offering Memorandum, subscribers are required to make a minimum non-refundable deposit of \$50,000, with the balance to be paid within 60 days of the deposit date. Based on discussions with officials from the Corporation and the escrow agent, the Corporation is still not enforcing these requirements. As at 30 September 1999, there are 23 units where the balance has been outstanding for more than 60 days of the deposit date and 31 units with no deposit.
- Included as part of the Confidential Offering Memorandum is a Distribution Agreement which outlines the terms and conditions under which the offering is marketed. In accordance with the terms of this Agreement, the distribution agent may charge the Corporation marketing expenses of up to 1% of the subscription proceeds (maximum \$350,000). The maximum 1% of proceeds received to date (\$135,000 up to 30 September 1999) has been charged and deducted by the distribution agent. The Corporation, on several occasions, has requested support for the marketing expenses from the distribution agent. However, as of 14 October 1999, no support has been provided by the distribution agent and therefore, the Corporation cannot be assured that it has paid for legitimate marketing expenses.

### **3.32 Newfoundland Government Fund Limited**

#### **Consulting and Professional Services**

Of the payments totalling \$1,566,601 to 31 December 1998, \$1,237,366 or 79% relates to consulting and professional services. The \$1,566,601 is comprised of expenditures of \$380,923 and deferred financing costs of \$1,185,678. In our last year's report we noted that the Corporation had not developed any policies regarding the selection, monitoring and evaluation of consultants. In addition, the Corporation could not provide information on how the various consultants were selected. During our current review Corporation officials indicated that the Corporation will follow Treasury Board Guidelines with respect to hiring consultants.

Since our last review, an additional \$548,374 in consulting and professional fees have been paid by the Corporation. However, almost all of these fees were paid for the continuing services of consultants selected in previous years, including the Escrow and Distribution agent which received \$508,106. No additional consulting contracts have been entered into by the Corporation since we raised this concern in last year's report.

#### **Corporation's Records**

Last year we reported that the Corporation's records were poorly maintained. During our review we noted that, although improvements have been made with respect to file management, there were still instances where investor files and subscription documentation were missing and could only be located after much effort. In addition, certain supporting documentation such as invoices were misfiled. We did note, however, that the Department of Industry, Trade and Technology has recently hired a staff member to, along with other responsibilities, ensure that all records of the Corporation are complete and properly maintained.

#### **Recommendations**

*The Corporation should comply with the Immigration Act (Canada) and Regulations.*

*The Corporation should ensure compliance with the Confidential Offering Memorandum and should consider all of its rights under the Memorandum.*

*The Corporation should continue efforts to properly maintain all records of the Corporation.*

### **3.32 Newfoundland Government Fund Limited**

#### **Corporation's Response**

##### ***Compliance with Canadian Immigration Regulations***

###### ***1. Investment of Subscription Proceeds***

*The Board of Directors of the Corporation, working with the Government departments involved, has approved a funding process which meets the investment objectives outlined in the Corporation's Offering Memorandum and complies with Federal Regulations. Citizenship and Immigration Canada have indicated their agreement with the arrangements and the Corporation has recently approved funding for health care centers to be constructed in Bonne Bay and on Fogo Island. On November 29, 1999 the Corporation invested available funds of \$9,450,000 in the two projects, thereby bringing the Corporation into compliance with Canadian Immigration Regulations.*

###### ***2. Audited Financial Statements***

*This matter has been rectified in that the financial statements in question have since been submitted to Citizenship and Immigration Canada. Steps have been taken to ensure this does not recur.*

##### ***Compliance with the Confidential Offering Memorandum***

###### ***(i) Repayment Account***

*The Corporation's banker has been contacted in writing once again and instructed to adjust the bank accounts to reflect the 20% allocation of proceeds deposited and maintained in the repayment account. Further, the bank has been asked to put in place a mechanism to address required changes to the account with future closings so that error does not recur. Review of monthly bank statements will be conducted by the Corporation to ensure this is done.*

###### ***(ii) Distribution of Unaudited Financial Statements***

*For future years, the Corporation will arrange to have unaudited financial statements prepared and issued for the period ended 30 June.*

###### ***(iii) Minimum non-refundable deposits***

*This matter will be reviewed with the escrow agent once again with the objective of resolving the matter.*

### **3.32 Newfoundland Government Fund Limited**

**(iv) Marketing fees**

*The distribution agent has provided the Fund with complete support materials relating to these fees.*

**Corporation's Records and Organization of Files**

*As noted, the Corporation's files have been arranged more properly and, with the addition of a staff member within the Department, this should not be a significant issue from this point forward.*



### 3.33 Royal Newfoundland Constabulary

#### Introduction

The Royal Newfoundland Constabulary was established in 1871. The mission of the Royal Newfoundland Constabulary is to work with communities in Newfoundland and Labrador to foster safe communities by providing quality, professional, accessible, timely and fair police services to all. The Royal Newfoundland Constabulary is responsible for policing three regions of the Province - the North East Avalon, Corner Brook and Labrador West. The population of these regions is approximately 205,000 (1996 census). In providing these services, the Royal Newfoundland Constabulary currently employs 310 police members and 75 civilian staff.

On 2 December 1997, a Select Committee of the House of Assembly was appointed to enquire into the arming policy of the Royal Newfoundland Constabulary, and report its findings to the House of Assembly by 31 March 1998. The Select Committee conducted research, viewed presentations by interested parties and held public hearings. The Committee tabled its report to the House of Assembly on 31 March 1998 which outlined the following recommendations:

1. Whereas the Royal Newfoundland Constabulary is an armed force and has been an armed force since 1991 and whereas the existing policy limits access to firearms, which are now kept in a locked box in the locked trunk of a police patrol vehicle, the Committee hereby recommends that the arming policy of the Royal Newfoundland Constabulary be amended to permit its members on operational duty to wear sidearms as part of their regular uniform.
2. The Committee further recommends that:
  - (a) The Chief of Police have discretion in the administration of the policy including discretion in assigning officers to operational duty and that in exercising this discretion the Chief of Police take into account the wishes of members of the Force who prefer not to be armed;
  - (b) police officers' sidearms be stored in a secure locker at the station when they are not on duty;
  - (c) a firearms audit acceptable to the Minister of Justice be performed annually and submitted to the House of Assembly; and
  - (d) the arming policy be reviewed at the end of five years by a Select Committee of the House of Assembly.



### 3.33 Royal Newfoundland Constabulary

As a result of the recommendations of the Select Committee on the Arming Policy of the Royal Newfoundland Constabulary, members on operational duty were permitted to wear sidearms commencing 14 June 1998. To provide specific direction to members on the control and usage of firearms, a revised Firearms Policy was also issued at this time. Figure 1 outlines the number of firearms maintained by the Royal Newfoundland Constabulary as of November 1999.

#### Scope and Objectives

One of the recommendations of the Select Committee on the Arming Policy of the Royal Newfoundland Constabulary was that a firearms audit acceptable to the Minister of Justice be performed annually and submitted to the House of Assembly. To comply with this recommendation, the Chief of Police requested my Office to conduct an audit of firearms. We completed our review in November of 1999. The objectives of the review were to:

- Determine whether the Royal Newfoundland Constabulary has adequate systems to record, monitor and secure its firearms inventory. This included determining, as recommended by the Select Committee, that sidearms be stored in a secure locker at the station when members are not on duty.
- Determine whether the revised Firearms Policy covered all relevant issues pertaining to the use and control of firearms.
- Determine whether the Royal Newfoundland Constabulary has adequate procedures to monitor members' compliance with the revised Firearms Policy and where appropriate, test compliance with this Policy.

Figure 1

#### Royal Newfoundland Constabulary Number of Firearms

|              | St. John's | Corner Brook | Labrador West | Total      |
|--------------|------------|--------------|---------------|------------|
| Handguns     | 344        | 51           | 24            | 419        |
| Shotguns     | 55         | 6            | 8             | 69         |
| Rifles       | 110        | 16           | 6             | 132        |
| <b>Total</b> | <b>509</b> | <b>73</b>    | <b>38</b>     | <b>620</b> |

Source: Royal Newfoundland Constabulary Inventory System

### **3.33 Royal Newfoundland Constabulary**

#### **Conclusions**

##### **Control Over Firearms and Ammunition**

The Royal Newfoundland Constabulary has established policies to provide for the management and control of its firearms and ammunition. Controls over firearms at the Royal Newfoundland Constabulary have significantly improved since our review of this area in 1996. Our review, however, identified a number of areas that require improvement. These include the following:

- The firearms and ammunition inventory system is not accurate. Our testing of this system indicated that not all firearms are recorded in the system and certain firearms recorded in the system had already been disposed of.
- Although the inventory system is a perpetual system (i.e. it is updated on an on-going basis), we determined that required adjustments, including dispositions and internal re-assignments of firearms and ammunition, are not always made on a timely basis. As a result, information on firearms and ammunition inventory is not always accurate and up to date.
- Segregation of duties over the purchasing, accounting and custody of weapons is not adequate. The same individual performs a number of incompatible duties including ordering and receiving of firearms related inventory, maintaining control over both the physical inventory and the inventory information system, and conducting annual inventory counts without any other officials present. Improper segregation of duties may result in errors or unauthorized transactions not being detected.
- In reviewing procedures for the annual physical count, we found that there is no documentation maintained on the results of the count or reasons for any required adjustments between the physical count and recorded inventory. In addition, discussion with Royal Newfoundland Constabulary officials indicated that although adjustments are made to the inventory system, there is no independent review or authorization of these transactions.

##### **Adequacy and Compliance of the Firearms Policy**

Our review indicated that the revised Firearms Policy of the Royal Newfoundland Constabulary is comparable to that of the other Canadian police jurisdictions and covered similar issues pertaining to the use and control of firearms.

### **3.33 Royal Newfoundland Constabulary**

Our review of compliance with the Firearms Policy indicated that members are not always complying with the policy. For example:

- Some of the plain clothes members on operational duty do not always wear sidearms as required by policy.
- Although policy requires that unloaded firearms be secured in the members personal firearms storage locker at Royal Newfoundland Constabulary facilities or in other approved locations when the member is not on duty, non-compliance with this policy is regularly observed during monthly inspections.
- Monthly inspections of service firearms are not being conducted as required by policy.
- A significant number of Royal Newfoundland Constabulary members have not requalified in firearms training every 12 months as required by policy. In addition, a significant number of members have not received use of force training as required by policy.

Although Use of Force Reports are required to be prepared by members and reviewed by supervisors to monitor members' compliance with Firearms and Use of Force Policies, we noted that Use of Force Reports are not always being completed and when they are completed, they do not always contain all required information such as member name and type of force used.

In addition, Use of Force Reports are not always submitted to the Use of Force Review Board on a timely basis.

#### **Findings and Recommendation**

##### **Inventory Management**

The Royal Newfoundland Constabulary has developed inventory control procedures to provide for the proper management of its firearms. These policies include such areas as the assignment of responsibility for control of weapons, the maintenance of a perpetual inventory system, the requirement for annual inventory counts and reports thereon, and procedures to update the inventory system for acquisitions, transfers, dispositions and any required adjustments. Our review of this area indicated the following:

### 3.33 Royal Newfoundland Constabulary

- Segregation of duties over the purchasing, accounting and custody of weapons is not adequate. The same individual performs a number of incompatible duties including ordering and receiving of firearms related inventory, maintaining control over both the physical inventory and the inventory information system, conducting annual inventory counts without any other officials present, and making all adjustments to the inventory information system. Improper segregation of duties may result in errors or unauthorized transactions not being detected.
- Procedures for inventory control require that an annual inventory count of weapons be performed by the Inventory Control Coordinator and a representative of the Internal Audit Division in April of each year. A report on this physical count is to be provided to the Director of Administration by 30 April. Our review found that the annual inventory count for fiscal 1999 was not performed until 22 June of 1999 and was conducted by the Range Master without any other officials present. The report was forwarded to the Director of Administration on 23 June 1999.
- In reviewing procedures for the annual physical count, we found that there is no documentation maintained on the results of the count or reasons for any required adjustments between the physical count and recorded inventory. In addition, discussion with Royal Newfoundland Constabulary officials indicated that although adjustments were made to the inventory system as a result of the count, no one reviewed or authorized these transactions.
- To ensure that all acquisitions are recorded in the inventory system, designated staff are required to forward information on weapons acquisitions, including receiving reports, to the Inventory Control Coordinator on a monthly basis or as otherwise requested. The Inventory Control Coordinator can then use this information to test the accuracy of the acquisitions when attending the annual inventory counts. Our review, however, indicated that a listing of these acquisitions and receiving reports are not being forwarded to the Inventory Control Coordinator as required nor, as previously indicated, is the Inventory Control Coordinator attending the annual inventory counts as required by policy.
- Although the inventory system is a perpetual system (i.e. it is continually updated), we determined that required adjustments, including dispositions or internal re-assignments of firearms and ammunition, are not always made on a timely basis. As a result, information on firearms and ammunition inventory is not always accurate and up to date.

### 3.33 Royal Newfoundland Constabulary

- Our review of reports produced from the inventory system indicate that although the report indicates an original quantity balance and what has been assigned or removed from the system, the report does not produce a total for balance on hand. This information would reduce the potential for human error when calculating the balance on hand and would also facilitate comparison of actual physical inventory to the inventory listing.
- With the exception of Labrador, we tested the accuracy of the inventory listings for firearms and ammunition by selecting a sample of physical inventory items and comparing this sample to the inventory system. We also selected a sample of items from the inventory system to ensure that the firearm was located where listed in the inventory system. During this testing we found that the inventory system is not accurate as outlined by the following instances:
  - 7 instances where serial numbers on firearms physically examined were not properly recorded in the inventory system. These firearms are antique weapons and the serial number is difficult to read. As a result, it appears that these are coding errors in the inventory system.
  - 3 instances where firearms examined were not recorded in the inventory system.
  - 3 instances where firearms are recorded in the inventory system; however, these firearms were previously donated to community organizations such as museums.
  - 16 instances where firearms were located in a different physical location than recorded in the system. These firearms were, however, located in secure areas within Royal Newfoundland Constabulary facilities.
  - There are 16 types of ammunition and we tested a sample of 12 which covered 9 of the 16 types. We determined that 7 physical counts did not agree to what was recorded in the inventory system and the differences could not be readily accounted for. Testing of ammunition also indicated two instances where what a member or assigned location physically had on hand did not agree to the inventory listing.



### **3.33 Royal Newfoundland Constabulary**

- Although there is a central inventory system of firearms and ammunition, detachments in Corner Brook and Labrador also produce their own inventory listings. A review of the most recent listings available indicated six discrepancies between these lists and the central inventory system.

#### **Firearms Policy**

The Royal Newfoundland Constabulary has a Firearms Policy to provide specific direction to members on the control and usage of firearms. Our review included a comparison of this policy with policies of other Canadian police jurisdictions. These jurisdictions included Halifax, Toronto Metro, Winnipeg, Brandon, Edmonton, Calgary, Vancouver, and New Westminster. We also reviewed procedures used by the Royal Newfoundland Constabulary to monitor members' compliance with the Firearms Policy which include inspections of firearms and firearms storage areas, review of reports prepared by members who have drawn firearms, and internal quality reviews over firearms. Where appropriate, we also tested compliance with this policy. Our review of these areas indicated the following:

##### **1. Adequacy of Policy**

Our review indicated that, in general, the revised Firearms Policy of the Royal Newfoundland Constabulary is comparable to that of the other Canadian police jurisdictions and covered similar issues pertaining to the use and control of firearms.

##### **2. Compliance with Policy**

A review of documentation maintained by the Royal Newfoundland Constabulary in monitoring compliance with the Firearms Policy, discussions with Royal Newfoundland Constabulary officials and testing of compliance with this Policy by my Office indicated that members are not always complying with the Firearms Policy. For example:

- Although the Firearms Policy requires all members assigned to operational duties to wear service firearms while on duty, Royal Newfoundland Constabulary officials indicate that members of the Criminal Investigation Division are sometimes leaving headquarters without arming themselves. We also observed several instances where firearms assigned to these members were secured in the designated locker at headquarters while the member was on duty but away from headquarters. The Royal Newfoundland Constabulary officials indicate that this breach of policy not only puts the officer in danger but also compromises the



### 3.33 Royal Newfoundland Constabulary

safety of his or her fellow officers as an unarmed officer cannot respond adequately to the assistance of another officer during an emergency.

- The Firearms Policy requires unloaded firearms to be secured in the members' personal firearms storage lockers at Royal Newfoundland Constabulary facilities or in other approved locations when the member is not on duty. To monitor compliance with this policy, the Range Master or his designate at other detachments conducts a monthly inspection of the firearms storage lockers. Any infractions with this policy are reported to the Divisional Commanders to follow up with the members. A review of these monthly inspection reports indicate that while the detachments in Corner Brook and Labrador as well as the satellite offices in Mount Pearl and Conception Bay South have never reported any infractions with this policy, the majority of inspections for the Patrol and Criminal Investigation Divisions in the St. John's detachment indicated some type of infraction. These infractions included instances where a firearm and/or ammunition was not stored in the locker even though the member was not on duty, stored firearms which were loaded, and the storage of personal articles in the firearms storage locker.

As part of our review, we attended a monthly inspection for the St. John's detachment and its satellite offices. During this inspection, we observed nine infractions similar in nature to those normally reported. We were unable to test compliance with the firearms storage policy at the satellite offices (i.e. Mount Pearl and Conception Bay South) as the Range Master does not have access to the firearms storage containers in these offices. Therefore, for those members not on duty we could not check the locked containers to determine whether the weapon was there and properly stored. We also conducted an unscheduled inspection at the Corner Brook detachment and noted two infractions at this location as well.

- In addition to inspection of the storage of firearms, the policy requires monthly inspection of the firearms themselves in accordance with guidelines established by the Inspections Officer. Our review indicated these guidelines have not yet been established and monthly firearms inspections are not being conducted. The Inspection Officer indicated he or his designate examines all firearms assigned to members during the quarterly personal inspections. Our attendance at one of these inspections indicated that while this inspection confirms that a member is carrying a firearm, it does not address whether the firearm is clean and in good working order as required by the Firearms Policy.

### 3.33 Royal Newfoundland Constabulary

- Firearms Policy requires that members requalify in both firearms training and use of force training at least every twelve months. While the policy also requires the Range Master to prepare a list of members who are qualified for firearms training, he could not provide us with such a list. We therefore selected a sample of 50 members and obtained the last training dates for firearms and use of force from various sources of information. Our review indicated the following:
  - only 18 of the 50 had requalified in firearms training in past 12 months;
  - only 20 of 50 had qualified in use of force training and no one has ever requalified. We do note, however, that of the remaining 30 members, 11 are scheduled for training in November and December of 1999.

As a result, a significant number of members are not requalified in firearms training every 12 months as required by policy. In addition, a significant number of members have not received use of force training as required by policy.

- The Firearms Policy requires that two Remington Model 870 12 gauge shotguns be contained in each Non Commissioned Officer vehicle for use in responding to certain threats. These firearms are to be removed at the end of each shift or during prolonged absences from the vehicle. Discussion with a number of these officers indicate that they do not carry these firearms in the trunk of their vehicle as these weapons cannot be secured in the current model of police vehicle. Instead, the firearm will generally be transported from headquarters to the required site by a Non Commissioned Officer.
- The Firearms Policy requires members to use loading/unloading ports that are located in firearms storage areas for the loading and unloading of firearms. As we were unable to observe this procedure, we could not determine whether members are complying with this policy. We do note, however, that the Tactics and Rescue Unit room is not equipped with a loading/unloading port although firearms are stored in this area.
- The Firearms Policy also requires that members be fully versed in the Use of Force Guidelines as outlined in the Use of Force Policy. These Guidelines provide guidance with respect to when it is appropriate to use force and the level of force required to be used in various situations. The Use of Force Policy requires that any time

### 3.33 Royal Newfoundland Constabulary

a member uses any type of force from simple restraint to discharging a firearm, a Use of Force Report must be filed.

These reports are reviewed by the member's immediate supervisor, the Divisional Commanders, and a Use of Force Review Board which has been established by the Royal Newfoundland Constabulary. Instances of force may also be reviewed by either the Public Complaints Commission or the Royal Newfoundland Constabulary's Internal Review Division upon the receipt of a complaint from a member or the general public.

Our review of this area indicated the following:

- We have been informed that there have been no complaints received by either the Internal Review Division or the Public Complaints Commission regarding use of firearms by members since the members started wearing sidearms in June of 1998.
- A review of the Use of Force Reports indicated that there were 288 reported incidents of force between June 1998 and October 1999. Of these 288 incidents, 36 related to firearms, 8 of which involved animals, 27 which involved drawing and/or pointing a firearm at a person and 1 which involved discharging a rubber bullet.

Members of the Use of Force Review Board indicate that the Board reviews all Use of Force Reports when the reports are received from the Divisional Commanders. Although the Divisional Commanders are submitting these reports to the Board, the reports are not always prepared on a timely basis. For example, at the end of our review in November 1999, reports from June 1999 to October 1999 for the largest division of the Royal Newfoundland Constabulary had not been submitted to the Board. As a result, the Board is not always reviewing the Use of Force Reports on a timely basis.

- The Use of Force Policy requires that the Use of Force Review Board meet quarterly. Although the Board indicated that it has met on a number of occasions, minutes were only kept for three such meetings since its inception in October 1998. We also noted that the first meeting was held to develop terms of reference and no Use of Force Reports were reviewed at this meeting. The minutes of

### 3.33 Royal Newfoundland Constabulary

these meetings do not contain sufficient detail to determine which Reports were reviewed or what decisions were made with respect to these reviews.

- A review of Use of Force Reports from June 1998 to October 1999 indicated that information required on these forms, including such information as type of force, member name, and reason why force was used, is not always being completed. We also noted that even though one of the most common types of use of force is handcuffing, there is no space designated on the Report to list this type of force. As a result, there may be insufficient information provided to enable supervisors and the Use of Force Review Board to assess the appropriateness of the use of force. We also found that, in general, these Use of Force Reports are not signed by the supervisors as evidence of their review of the form.

During a review of these Reports, we found instances where one member indicated on his or her Report that another member was present during the incident but there was no Report filed by the other member. We also noted that the Chief of Police and the Divisional Commanders have written memos to the members emphasizing the necessity of filing these Reports but there is still evidence that not all instances are being reported. The Use of Force Review Board also expressed concern regarding the lack of Use of Force Reports completed by the Criminal Investigation Division. In particular we noted that the Criminal Investigation Division had only reported two incidents of force since June of 1998.

- The Chief of Police has directed all Divisional Commanders to prepare a summary of statistics on the use of force on a monthly basis. The Divisional Commander of the Criminal Investigation Division only prepares a summary if there were use of force incidents. As a result, we could not determine whether a report was just missing or there was no use of force incidents that month.

A review of the summaries that were prepared indicated that they are not always being prepared on a timely basis and sometimes do not contain all relevant information that was contained on the Use of Force Report such as member name, and certain instances where force was used. We also found that Divisional Commanders' interpretation of how

### 3.33 Royal Newfoundland Constabulary

to determine the number of uses of force resulting from an incident varies. As a result, statistics being accumulated on the incidents and types of use of force may not be accurate.

During our review, we noted that the Internal Audit Division of the Royal Newfoundland Constabulary completed a quality review of the Firearms Policy in October 1998. The main findings of this review included that inspections of firearms storage lockers and service firearms were not being conducted on a monthly basis, the Inspections Officer had not developed any guidelines for the inspection of service firearms, there was a lack of documented inspections by supervisors, some policy and procedures manuals did not include the Firearms Policy, and the Range Master at that time was not fully versed in using the computerized inventory system. Some but not all of these issues have been addressed.

#### **Recommendation**

*The Royal Newfoundland Constabulary should review the observations outlined in this report and take appropriate action.*

#### **Royal Newfoundland Constabulary's Response**

*While the Royal Newfoundland Constabulary (RNC) agrees with the majority of the observations contained in the Auditor's report, it feels that there are a number of issues that require a more detailed response. As the findings and recommendations of the report focused on the three critical areas of Inventory Management, Firearms Policy and Training, the RNC has formulated its response along these lines.*

#### **Inventory Management**

*Notwithstanding the concerns noted with respect to Inventory process, the Executive of the RNC is confident that all firearms under its control are accounted for and secured. It would appear that this fact is further supported in the conclusion section of the report where it is noted that controls over firearms "have significantly improved since our review in this area in 1996". The observations related to firearms management, specifically as they pertained to segregation of duties, periodic inventory counts, and various inaccuracies in the inventory listings have been noted. A senior officer with the Force's Audit Services Section will be directed to address the concerns identified in your report and initiate the required remedial action early in 2000.*



### **3.33 Royal Newfoundland Constabulary**

#### ***Firearms Policy***

*While the RNC is pleased that the report referenced the adequacy of our revised Firearms Policy, given the many complexities associated with this issue, the Force will continue to monitor its policy to ensure that it reflects "best practices" in this area.*

*The concerns expressed in the audit dealing with compliance with policy, specifically as this pertained to regular formal inspections and related reports, security of officer's firearms when not on duty etc. have been duly noted and are in the process of being addressed. While compliance with policy is the responsibility of all members, management and supervisory staff will continue to closely monitor this area in light of the issues raised.*

*Towards this end a senior commissioned officer has been tasked to ensure that detailed inspections of both the firearms and the storage of same are carried out in accordance with accepted practices. While the Force appreciated the Report's reference to the fact that inspections are conducted, it will be the responsibility of the senior officer to ensure that the inspection criteria is articulated to all personnel and that the inspections are regularly scheduled and documented.*

#### ***Use of Force/Firearms Training***

*The concerns raised in this section of the report are currently being addressed on an ongoing basis. While we acknowledge delays in implementing the new Use of Force training model as a result of mechanical problems with our range, the unavailability of our gym etc., it should be noted that all members assigned to operational duty are qualified in the use of firearms. Furthermore, as of December 31, 1999, 259 members out of a total of 310, have received the enhanced Use of Force/Firearms training. The remaining operational personnel will receive this training by February, 2000. To meet the aggressive requalifying schedule for the Use of Force/Firearms training, additional resources will be assigned to this area.*

*As you are aware our Range Master has been selected to sit on a national committee, under the auspicious of the Canadian Police College, to develop National Use of Force/Firearms training standards. This participation will ensure that the RNC is kept abreast in this important facet of police training.*



### 3.33 Royal Newfoundland Constabulary

*The Force acknowledges certain logistical and scheduling problems associated with the operations of the Use of Force Review Board. However, it must be emphasized that members of the Review Board are provided with copies of all reported incidents of use on a timely basis for their individual review and feedback. The implementation of the Review Board by the RNC meets or exceeds national best practices and is a further indication of our commitment to ensuring that all members conform with the highest standards expected of police officers in the Use of Force, particularly as this applies to the use of firearms.*



### 3.34 Municipal Debt

#### Introduction

#### Departmental Overview

The Department of Municipal and Provincial Affairs is responsible for matters relating to local government, municipal financing, property assessment, urban and rural planning, infrastructure development and engineering, and the coordination of emergency planning for municipalities. Figure 1 details the Department's current and capital expenditures for the year ended 31 March 1999.

Two main activities within the Assistance and Infrastructure Program are Debt Servicing (current) representing Provincial Government contributions for interest charges on municipalities' outstanding debt and Municipal Infrastructure (capital) representing Provincial Government contributions for the principal portion on municipalities' outstanding debt. As indicated in Figure 1, \$28.5 million was paid by the Provincial Government towards interest charges on municipalities' outstanding debt and \$38.3 million was paid by the Provincial Government towards the principal portion of municipalities' outstanding debt.

**Figure 1**

**Department of Municipal and Provincial Affairs  
Current and Capital Expenditure  
Year Ended 31 March 1999  
(\$ Millions)**

|                                              | Current | Capital | Total    |
|----------------------------------------------|---------|---------|----------|
| <b>Assistance and Infrastructure</b>         |         |         |          |
| Debt Servicing                               | \$ 28.5 |         |          |
| Municipal Operating Grants                   | 24.7    |         |          |
| Special Assistance                           | 9.3     |         |          |
| Regional Cooperation Initiatives             | 0.1     |         |          |
| Municipal Infrastructure                     |         | \$ 38.3 |          |
| Canada-Newfoundland Infrastructure Program   |         | 6.1     |          |
| Water and Sewer Servicing - Coastal Labrador |         | 2.9     |          |
| Sub-total                                    | 62.6    | 47.3    | \$ 109.9 |
|                                              |         |         |          |
| Municipal Protection Services                | 1.2     | 0.3     | 1.5      |
| Executive and Support Services               | 3.4     |         | 3.4      |
| Services to Municipalities                   | 4.7     |         | 4.7      |
| Department Total                             | \$ 71.9 | \$ 47.6 | \$ 119.5 |

Source: 1999 Public Accounts

### 3.34 Municipal Debt

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| <b>Department Total</b>                      | \$ 71.9 | \$ 47.6 | \$ 119.5 |

Source: 1999 Public Accounts

### 3.34 Municipal Debt

Total municipal debt is comprised of debt owed by municipalities to the Newfoundland Municipal Financing Corporation and to banks. Newfoundland Municipal Financing Corporation is a Crown corporation created by the *Municipal Financing Corporation Act* to provide long-term financing for the capital requirements of municipalities through the issuance of securities and relending the funds to municipalities. The debt incurred by municipalities is used to finance such infrastructure projects as water and sewer systems, and roads. The majority of this debt is cost shared between the Province and the municipalities involved.

#### Background

We have previously reported to the House of Assembly on municipal debt as follows:

Our 1994 Annual Report included a report on the monitoring and control of municipal debt. Our review indicated that: the Department did not adequately monitor and control the financial activities of municipalities as required by legislation; debt owed by municipalities to the Newfoundland Municipal Financing Corporation had increased by approximately 30% over the previous six years; annual repayments of debt and related interest costs had increased by 40% over the previous six years; arrears on debt owed by municipalities indicated that many municipalities were experiencing difficulties in paying their debt obligations and the Department did not have current financial information to ensure municipalities did not incur excessive or unmanageable debt obligations.

Our 1995 Annual Report included a report on the municipal infrastructure program. Our review indicated that: many municipalities were in poor financial condition; were economically dependent on the Province; a significant number of municipalities had reached the maximum annual repayment amount of water and sewer debt they were required to finance with any additional debt incurred to be the responsibility of the Province; many municipalities were not in a position to determine their financial condition at intervals frequent enough to allow for timely corrective action; most of the 20 councils examined had a general idea of road conditions but few had reliable and objective assessments of water and sewer system condition and there was no evidence of any correlation between the direction for infrastructure growth in the Province as provided for under the Province's Strategic Economic Plan and the actual development of infrastructure as approved by Government.

Our 1995 Annual Report also included a report on the Newfoundland Municipal Financing Corporation. Our review indicated that management practices were not adequate to provide reliable and timely information to management and the Board of Directors of the Newfoundland Municipal Financing Corporation. In particular: there was

### **3.34 Municipal Debt**

inadequate information on the financial condition of the Corporation; cash flow forecasting was inaccurate and did not provide reliable information for decision making purposes; and the Corporation had not undertaken adequate strategic planning to determine its future operation.

#### **Scope and Objectives**

We completed our review of municipal debt in May 1999. The review included an assessment of the level of municipal debt within the Province and the identification of policies and procedures in place within the Department of Municipal and Provincial Affairs to monitor and control the level of debt incurred by municipalities. Our objectives were to determine:

- the current level of municipal debt and the changes in debt;
- the nature and objectives of the Department's municipal debt strategies and the changes in these strategies; and
- whether the systems and procedures in place within the Department are adequate to monitor municipal debt.

Our review included interviews with Department officials and a review of relevant authorities, plans, policies and procedures, reports and Departmental information.

#### **Conclusions**

Our review disclosed that serious concerns remain with respect to the level of municipal debt, the ability of municipalities to administer this debt, and the monitoring of debt by the Department of Municipal and Provincial Affairs. Specifically, our review disclosed the following:

- The Department could not provide us with the amount of total municipal debt as at 31 December 1998 for the 290 municipalities in the Province, including the three cities. At the time of our review, the Department's records indicated the amount was in excess of \$497 million. Our review of the database of information containing data on total municipal debt revealed that the information was inaccurate and incomplete. Our testing included a review of available audited financial statements for the year ended 31 December 1998 as well as a review of information submitted by the various chartered banks. In comparing this information to the database, several differences and omissions were detected.



### 3.34 Municipal Debt

- While total debt is increasing, municipal debt financed by the Newfoundland Municipal Financing Corporation is decreasing while the municipal debt financed by chartered banks is increasing. Newfoundland Municipal Financing Corporation debt has decreased from \$445 million as at 31 December 1994 to \$330 million as at 31 December 1998, a reduction of \$115 million.

While municipal debt financed by chartered banks is increasing, the Department does not maintain complete and accurate information on this debt. As a result, the Department does not know the total financial condition of all municipalities.

- Provincial assistance to municipalities, which includes funding for debt servicing costs (principal and interest) and municipal operating grants, has been decreasing while municipal debt costs are increasing. Assistance and infrastructure funding has decreased from \$133 million in 1994-95 to \$110 million in 1998-99.
- Although total debt to the Newfoundland Municipal Financing Corporation has decreased by \$115 million over the last four years, arrears to the Newfoundland Municipal Financing Corporation have increased significantly from \$10.8 million as at 31 December 1993 to \$19.2 million as at 31 December 1998. Since the Department does not have information on all municipal debt at chartered banks, they do not know the extent of arrears, if any.
- For those municipalities for which taxation information was available, mil rates for property taxes ranged from 2.5 mils to 17 mils, water and sewer rates ranged from \$30 to \$420 per household, and poll tax rates ranged from \$20 to \$300.
- The existing *Municipalities Act* outlines a framework of accountability by municipalities to the Department of Municipal and Provincial Affairs. Municipalities are not complying with this framework. For example, most municipalities do not submit their annual budgets by the statutory deadline of 31 December. In addition, 12 municipalities had not submitted the required 1997 financial statements at the time of our review. Financial statements for 1998 were not due to be submitted to the Department by the municipalities at the time of our review and therefore were not generally available. The Department should enforce compliance with the *Municipalities Act* so that it will have the information that is required to monitor the financial condition of the municipalities.

### 3.34 Municipal Debt

#### Findings and Recommendations

#### Level of Municipal Debt

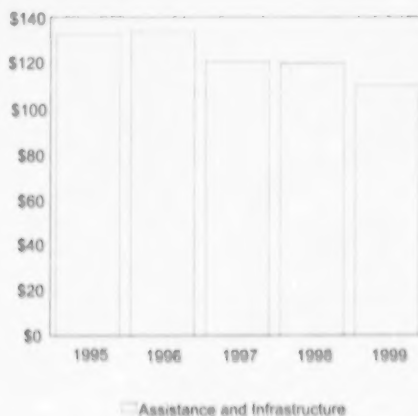
The Department could not provide us with the amount of total municipal debt as at 31 December 1998 for the 290 municipalities in the Province, including the three cities. Our review of the Department's information on total municipal debt indicated that the information was inaccurate and incomplete. Our review included an assessment of available audited financial statements as well as a review of information submitted by the various chartered banks. In comparing this information to the Department's internal information, several significant differences and omissions were detected. For example, debt totalling approximately \$100 million is included in the 1998 financial statements of the City of St. John's but is not included in the Department's records. At the time of our review, the Department's records indicated that total municipal debt was in excess of \$497 million of which \$330 million was borrowed from the Newfoundland Municipal Financing Corporation while \$167 million was borrowed from chartered banks.

#### 1. Provincial Assistance

Provincial assistance and infrastructure funding to municipalities has decreased significantly over the past few years, from \$133 million in 1994-95 to \$110 million in 1998-99. Provincial assistance to municipalities includes funding for debt servicing costs (principal and interest) and municipal operating grants. Figure 2 provides information on provincial assistance to municipalities for the years ended 31 March 1995 through 31 March 1999.

Figure 2

**Department of Municipal and Provincial Affairs  
Assistance and Infrastructure Expenditures  
Years Ended 31 March  
(\$ Millions)**



Source: Public Accounts of the Province

### 3.34 Municipal Debt

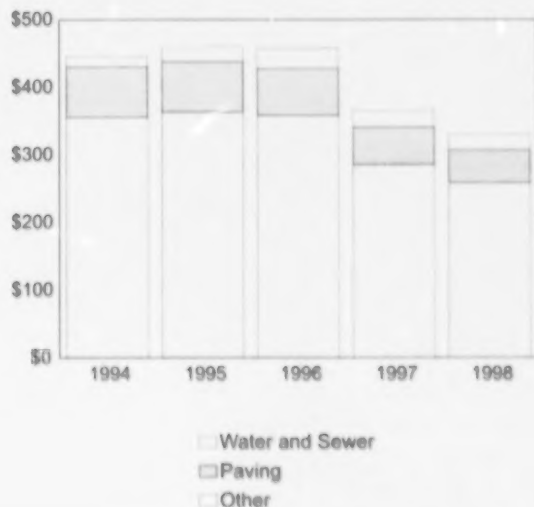
In addition to funding received from the provincial Government, municipalities also obtain funding through taxation. Information on file at the Department for 245 of the 290 municipalities indicated that the mil rates for property taxes ranged from 2.5 mils to 17 mils. For those municipalities that have water and sewer taxes and poll taxes, levies ranged from \$30 to \$420 per household for water and sewer and from \$20 to \$300 for poll taxes.

#### 2. NMFC Debt and Arrears

Although total municipal debt has increased significantly, municipal debt financed through the Newfoundland Municipal Financing Corporation has decreased by approximately \$115 million from the period of 31 December 1994 to 31 December 1998. The municipal debt financed through the Newfoundland Municipal Financing Corporation has been decreasing annually since 1996, with the largest decreases in 1997 (20.2%) and 1998 (9.7%). A major reason for this decrease is that many municipalities have been refinancing their outstanding debt at the Newfoundland Municipal Financing Corporation with chartered banks. Figure 3 provides a summary of debt owed to the Newfoundland Municipal Financing Corporation by municipalities from 1994 to 1998.

Figure 3

**NMFC Debt  
31 December  
(\$ Millions)**



Source: Database maintained by the Department of Municipal and Provincial Affairs

### 3.34 Municipal Debt

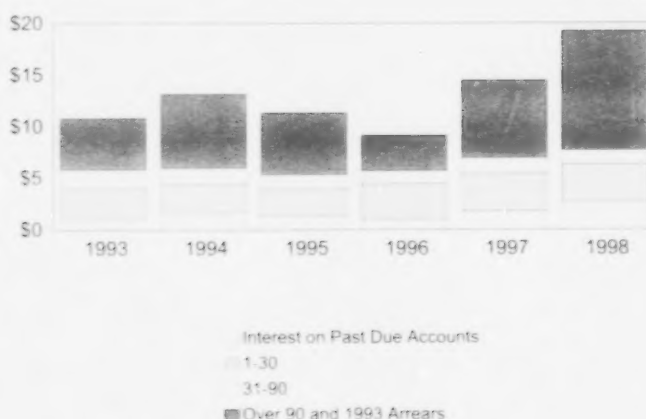
Although the amounts owing to the Newfoundland Municipal Financing Corporation have decreased from \$445 million in 1994 to \$330 million in 1998, the amount in arrears has increased significantly from \$10.8 million as at 31 December 1993 to \$19.2 million as at 31 December 1998. Figure 4 provides information as to total arrears to the Newfoundland Municipal Financing Corporation and the composition of these arrears for the calendar years from 1993 to 1998.

Our review of the changes in NMFC arrears from 1993 to 1998 indicated the following:

- 184 municipalities had arrears as at 31 December 1993 totalling \$10.8 million and 140 municipalities had arrears as at 31 December 1998 totalling \$19.2 million;
- 97 of the 184 municipalities in arrears for 1993 had increased their arrears in 1998; and a further 25 municipalities which were not in arrears in 1993 had arrears in 1998; and
- the 87 municipalities which had decreased their arrears had done so in part (18 municipalities) or entirely (69 municipalities).

**Figure 4**

#### NMFC Arrears 31 December (\$ Millions)



Source: Newfoundland Municipal Financing Corporation

### **3.34 Municipal Debt**

#### **Departmental Strategy**

The Department has indicated that its strategic plan along with its Departmental Plan for 1999-2000 and the decisions made earlier under Program Review are serving to set the vision and mission for the Department, define its core lines of business and address, in part, the problems associated with municipal debt.

Based on this strategic planning initiative, the Department has identified and is addressing four major challenges and strategic issues, as follows.

##### **1. Adequacy of Municipal Infrastructure**

The Department has indicated that the delivery of capital works should be more effective with regard to costs, targeting, affordability, and suitability. It has also recognized that the requirements for and cost of providing for all municipal infrastructure needs far exceeds the Province's capacity to supply funding.

At the time of our review, the Department estimated that the cost to fund all water and sewer system requirements would total approximately \$3 billion (\$1.5 billion for water and sewer connections, \$1 billion for water treatment and \$535 million for waste treatment). As well, it was estimated that 1,250 km of the Province's 4,200 km of municipal roads needed upgrading at an estimated cost of \$125 million.

In relation to water and sewer systems, the Department estimated the cost of water and sewer connection per household to be approximately \$28,000, with an additional \$9,500 per household to provide water and waste treatment. The Department has also indicated that there were 117 boil orders in effect on various water supplies during the year ended 31 March 1999 with at least 1 of these being in effect for 13 years, and 29 being in effect for more than 5 years.

The Department has also indicated that there is an inadequate level of capital works planning at the municipal level and that some municipalities have only partially completed infrastructure systems. The present approach addresses only currently identified projects and is susceptible to shifting priorities and inadequate analysis.

##### **2. Problems with Municipal Financing**

The Department recognizes that many municipalities are experiencing serious financial problems. Some areas of concern identified by the Department include the reduction in Municipal Operating Grants, insufficient municipal generated taxation revenues, inflexible financial support, and a lack of accountability.

### **3.34 Municipal Debt**

Although there is a requirement for municipalities to balance their budgets, many of them have significant accumulated deficits. In addition, financial documents such as budgets and audited financial statements are not always being received by the Department thereby making it impossible to monitor the financial condition of the province's municipalities.

Debt servicing costs are the largest expenditure items in municipal budgets. In the past, the ability of the local tax base to support developments in municipal infrastructure and related services was not a major criterion as continuing government grants and subsidies were assumed.

#### **3. Need to Strengthen Local Governments**

The Department has indicated that the lack of financial control and effective monitoring at municipalities has contributed to the overall municipal debt problem being faced by many municipalities. The Department recognizes the need for training key people within the municipal government structure.

#### **4. Changing Role of Department**

The Department sees its role as shifting from one of a provider to that of a facilitator and policy maker. In the past, focus had been on operational activities and the Department recognizes it had not developed strong policy, planning or analytical capabilities. Crisis management skills had been utilized at the expense of planning skills.

#### **Monitoring of Municipal Debt**

The existing *Municipalities Act* outlines a framework of accountability by municipalities to the Department of Municipal and Provincial Affairs, including provisions relating to budgeting, financing and general municipal operations. The Municipal Finance Division within the Department is responsible for monitoring and advising municipalities in these matters.

The Municipal Finance Division has developed a database to record information relating to municipal operations. Information input to this database is used to monitor municipal debt. An analysis of the database was completed to determine the extent to which the Department is ensuring compliance with the accountability provisions of the *Municipalities Act*. The results are as follows:



### 3.34 Municipal Debt

#### 1. Budgets

##### (a) Preparation and Adoption of Budget

Section 74(1) of the *Municipalities Act* states that council shall, not later than 90 days after the day on which the council takes office in the 1st financial year, and not later than December 1 in each succeeding year, prepare and adopt a budget containing estimates of the revenue and expenditure of the council for the next financial year and a statement showing the rate of tax that will be imposed during that year.

Section 74(2) of the *Act* states that the budget shall be in the form that the Minister may prescribe and a copy shall be sent to him or her on or before December 31 in each year, or in the case of a new council, within 30 days of its adoption.

Our review of information maintained by the Department as well as discussions with Departmental officials disclosed the following:

- As of April 1999, 90 of 290 municipalities had not submitted their 1999 budgets, 177 had submitted their budgets after the 31 December deadline and 23 were submitted on time; and
- As well, 45 of 290 municipalities had not submitted their 1998 budgets, 163 were received late with budgets for the remaining 82 municipalities being submitted on time.

##### (b) Balanced Budgets

Section 75 of the *Act* states that the anticipated revenues and proposed expenditures of the council shall balance.

Our review of the Municipal Finance Division's database disclosed that 18 of the 1997 budgets and 7 of the 1998 budgets presented to the Department did not balance.

##### (c) Expenditures in Excess of Budget

Section 78 of the *Act* states that a council shall not without the approval of the Minister incur, enter into, contract, or become liable for an expenditure or indebtedness beyond or in excess of the estimated amount of expenditure set out in the adopted budget or revised budget.

### 3.34 Municipal Debt

Our review of the Municipal Finance Division's database disclosed that for the 221 municipalities which had submitted both their 1997 budgets and 1997 financial statements, 145 had actual expenditures, per their financial statements, which exceeded the total expenditure reflected in their budgets. Financial statements for 1998 were not available at the time of our review. Department officials advised that approval of the Minister was not obtained relating to each of these excess expenditures.

#### 2. Financial Statements

Section 87 of the *Act* states that the auditor shall complete and submit the report on his or her audit within 5 months of the end of the financial year that he or she is auditing. Section 88 of the *Act* further states that the council shall send a copy of the audit to the Minister within 30 days of its receipt.

Section 84 of the *Act* states that the Minister may, by order, waive the requirement of an audit for a council where he or she is satisfied that an inspection by the officials of his or her Department is sufficient to ensure adequate financial control and accountability.

Our review disclosed that of the 290 municipalities, 34 were exempted from audit by the Minister as permitted by the *Act*. Of the 256 municipalities required to submit audited financial statements for 1997, 244 had submitted these statements. We could not determine whether these audited financial statements were received by the Department in accordance with the deadline established under the *Act*. As noted above, financial statements for 1998 were not generally available at the time of our review.

#### Recommendations

*The Department should continue with the implementation of its strategic planning initiatives in a timely manner.*

*The Department should ensure that municipalities are in compliance with the Municipalities Act and that all financial information required to adequately monitor municipal operations is tracked to provide for timely analysis for decision making.*

### 3.34 Municipal Debt

#### Department's Response

*The Municipal Finance Division is implementing a monitoring system to track the status of budget and financial statement submissions by municipalities. The Department will place greater priority on encouraging municipalities to submit the necessary financial documents on a timely basis. Current work on increasing municipal accountability requirements will help to achieve this status.*

*With respect to Municipal Debt, since the Department's Municipal Finance Division implemented the non-guaranteed loan database in 1998, there has been steady progress in improving and updating the information. The Department has arranged for all major banks to submit quarterly reports regarding any municipal debt that they carry. This information is then compared with the financial statements provided to the Department by Municipalities to ensure that the information received is accurate and complete.*

*With regard to the total amount of municipal debt and the arrears of debt servicing, the Department's records indicate that debt servicing is dropping each year due to the fact that the amount of debt maturing is greater than the amount of debt servicing that is being approved each year. This trend will continue and the overall municipal debt situation should show an improvement over the next few years. Other factors that should alleviate the arrears situation are as follows:*

- *Municipal Operating Grants will not decrease below the 1999 level for at least the next two years.*
- *Municipalities are increasing their tax rates to acceptable levels.*
- *The impact of the Debt Relief Program.*

### **3.35 Debt Relief Program**

#### **Introduction**

The Department of Municipal and Provincial Affairs is responsible for matters relating to local government, municipal financing, assessment, urban and rural planning, development and engineering, and coordination of emergency planning for municipalities.

During 1996-97, the Department introduced a Debt Relief Program to assist municipalities in debt refinancing or debt restructuring. The Program is intended to assist municipalities in poor financial condition, determined by a comprehensive review of individual municipalities' past performance in relation to financial activities, with consideration of other factors including economic conditions, taxing capacity, and out-migration.

As at 31 March 1999, Government had advanced a total of \$17 million in Program funding to the Newfoundland Municipal Financing Corporation, to be held in a reserve for use in mitigating arrears with respect to municipal loans. The amount of the allocation is determined through assessments completed by the Department with final approval from the Newfoundland Municipal Financing Corporation. Of the \$17 million in Program funding, approximately \$6.1 million had been allocated to 13 municipalities as at 31 March 1999, leaving an unallocated balance in the reserve fund of \$10.9 million.

#### **Scope and Objectives**

We completed our review of the Debt Relief Program in September 1999. Our objectives were to:

- determine the nature and objectives of the Program;
- determine whether Program guidelines were in place and were being complied with;
- review how the Program is administered and how funds are allocated; and
- assess whether monitoring and reporting mechanisms have been established to measure success towards achieving Program objectives.

### 3.35 Debt Relief Program

#### Conclusions

Our review disclosed that:

- Guidelines for the Program, defining the Program's objectives, organizational structure, processes, and expected outcomes have not been formally established. Draft Program guidelines did exist and were well structured; however, they were not formally approved by the Department. As well, criteria which would determine how much funding a municipality would be entitled to under the program, have not been well defined and properly approved.
- We were advised that the draft guidelines were to be in effect for the period covered by our review; however, certain provisions contained in the draft guidelines were not complied with.
- In April 1997, the Department estimated that it would complete a review of 170 affected municipalities by 30 October 1998. By January 1999, Departmental reviews had commenced with only 112 municipalities, with negotiations being finalized for only 47 of these 112. The Department indicated that the revised estimate for completing the remaining reviews is March 2000.
- The draft guidelines indicated that *"The municipalities that will be targeted are those that spend more than 30% of their municipal revenues on debt."* As well, it is indicated that *"Order of priority will be given to municipalities with the highest debt to revenue ratio but priority may change to accommodate special circumstances."* Our review indicated that the municipalities were not reviewed in this order. For example, of the 20 municipalities with the highest ratio, only 16 had been reviewed as at January 1999 while the review of the remaining 4 had not commenced.

One of the first reviews undertaken was for the Town of Harbour Grace, which was listed as number 153 on the June 1997 list of priority and which had a debt to revenue ratio of less than the 30% targeted under the draft guidelines.

- The negotiated agreements which were signed with the municipalities required that the municipalities must meet certain conditions to access Program funding, including such conditions as raising municipal taxes and not applying for future capital works funding for up to 15 years. In the case of tax increases, the tax rates established by the Department are not consistent and vary by municipality.

### 3.35 Debt Relief Program

- Under the Debt Relief Program, a comprehensive review of each municipality was to be performed incorporating a number of factors, including past performance and the ability to raise revenues and service debt. The analyses completed by the Department did not typically address future capital works and funding requirements. In order for restructuring to be viable on a long term basis, it would be expected that these factors would be taken into account.
- Our review disclosed that a detailed financial analysis was not completed for all municipalities which were reviewed and received funding. Of the 13 municipalities which received funding, the Department did not complete a detailed financial analysis for 2. These 2 municipalities were assisted under the Program with debt relating to water and sewer infrastructure projects which were only partially completed in the past. Due to the fact that the systems were not completed, the intended services were not being provided to the communities involved. Such systems are considered as dry lines.

For one municipality, the Department considered there was no need to complete a detailed financial analysis as it felt the town was in good financial position. It was indicated that the decision to assume the Council's share of the debt was based on "principle" rather than the financial position of the town as would be expected based on the draft Program guidelines and on the review of other agreements under the Program.

- It is understood from discussions with Departmental officials that the 30% debt to revenue ratio identified in the guidelines was a target and was intended to identify municipalities in need of assistance. However, the lack of definitive indicators as to qualifications for assistance resulted in a process which was not transparent to the various stakeholders involved. In the case of assistance provided under the debt relief program, many municipalities did not receive funding even though their debt to revenue ratio exceeded the 30% identified in the guidelines. As well, many municipalities that did receive funding were left with debt to revenue ratios exceeding 30%.
- Debt Relief Program agreements between the Department and individual municipalities were signed by the Department and the municipalities involved prior to receiving approval from the Department of Finance for allocation from the reserve fund. The Deputy Minister of Finance expressed concerns over such prior approvals in a letter to the Deputy Minister of Municipal and Provincial Affairs.



### 3.35 Debt Relief Program

- Monitoring and reporting mechanisms established to measure success towards achieving Program objectives have not been complied with. In particular, the Debt Relief Program Review Committee indicated to be in place to ensure the program objectives are met, did not hold regular meetings or keep related minutes. Also, although the draft guidelines indicated a need to monitor the action plans of the individual municipalities, there was no related monitoring strategy in place. As well, other than through ministerial statements, no periodic overview reports were made on the objectives of the Program for the House of Assembly and other stakeholders.

#### Findings and Recommendations

##### 1. Nature and Objectives of the Debt Relief Program

The Debt Relief Program was introduced in 1996-97 to assist municipalities in poor financial condition. Financial condition was to be determined by a comprehensive review of individual municipalities' past performance in relation to financial activities, with consideration of other factors including economic conditions, taxing capacity, and out-migration.

General objectives of the Debt Relief Program, as identified in draft Program guidelines, are outlined in Figure 1.

The municipalities targeted under the Program were generally those which spent more than 30% of their municipal operating grant and tax revenues on debt servicing costs. In April 1997, the Department estimated that 170 municipalities met the target criteria and therefore would be reviewed to determine eligibility under the Program.

Figure 1

#### Debt Relief Program Program Objectives

*To create strong financial independence, stability and accountability among municipalities.*

*To serve to strengthen local government in the Province.*

*To ensure the future viability of rural Newfoundland and Labrador.*

### 3.35 Debt Relief Program

#### 2. Program Guidelines

Although guidelines defining the Program's objectives, organizational structure, processes, and expected outcomes were drafted, these guidelines were not formally approved. Officials at the Department provided a copy of the draft Program guidelines, dated 28 April 1997, which were indicated to be in effect for the period covered by our review.

The draft guidelines were well structured; however, they were not formally approved and the criteria which were used to assess whether municipalities were to receive funding and the amount they were to receive were not well defined.

Our review disclosed that the Department had not complied with the following provisions of the draft guidelines:

- **Debt Relief Program Review Committee**

The draft guidelines provide that the Debt Relief Program Review Committee is to consist of the Executive of the Department and the Program Manager. The Committee's responsibility is to ensure the program objectives are met, issues resolved, progress reviewed, and guidance and direction given. Our review disclosed there were no regular meetings held or minutes kept relating to this Committee. Although the Program Manager did prepare some reports on the status of the Program, there was no evidence that reports on the objectives of the Program were required by or presented to the Committee.

- **Approved work plan and project schedule**

The April 1997 draft guidelines indicated that reviews of the estimated 170 municipalities under the Debt Relief Program would be completed at the rate of 8 to 10 municipalities per month, with reviews for all affected municipalities to be completed by October 1998. The major objective of the work plan was to compile and analyze sufficient financial data for each municipality in order to provide recommendations to allow the municipality to become more self-reliant and less dependent on Government.

Our review indicated that as at January 1999, Departmental reviews had commenced for 112 municipalities, with negotiations being finalized for only 47 municipalities. Of these 47, the Department determined that 15 required some assistance. The Department indicated that the revised estimate for completing the remaining reviews is March 2000.

### 3.35 Debt Relief Program

The draft guidelines indicated that *"The municipalities that will be targeted are those that spend more than 30% of their municipal revenues on debt."* As well, it is indicated that *"Order of priority will be given to municipalities with the highest debt to revenue ratio but priority may change to accommodate special circumstances."* Our review indicated that the municipalities were not reviewed in this order. For example, of the 20 municipalities with the highest debt to revenue ratio, only 16 had been reviewed as at January 1999 while reviews for the remaining 4 had not commenced.

One of the first reviews undertaken was for the Town of Harbour Grace, which did not have a debt to revenue ratio of 30% and was listed as number 153 on the June 1997 priority list.

- **Action plans**

The draft guidelines provide for negotiation and *"...acceptance of an Action Plan that will permit the municipality to operate in a manageable financial environment that will provide stability in its financial affairs."* There were to be signed agreements between the Department and the municipalities receiving funding as to the course of action necessary to strengthen the financial position of the municipality. Our review indicated that future infrastructure requirements of the municipalities were not addressed in these action plans. As a result, significant related financial commitments, which could impact the future financial stability of the municipality, have not been factored into these action plans.

Municipalities which were reviewed but did not receive funding under the Program were advised by the Department as to how their financial position could be improved.

- **Program monitoring and reporting strategy**

Although the draft guidelines indicated a need to monitor the action plans of the individual municipalities, and to periodically provide overview reports on the progress of the program, there was no related monitoring or reporting strategy in place.

### **3.35 Debt Relief Program**

#### **3. Program Administration and Funding Allocation**

##### **(a) Program Testing**

To test the consistent application of the Debt Relief Program, we reviewed all 13 municipalities which had received funding under the program as at 31 March 1999 and 4 municipalities which had been assessed by the Department as requiring no funding.

Our review of these 17 municipalities, indicated the following:

- with the exception of Harbour Grace, the financial analysis of the remaining 16 municipalities did not address future capital works and funding requirements. In order for restructuring to be viable on a long term basis, it would be expected that future capital work requirements and related financing would be taken into account;
- detailed financial reviews were not completed for all municipalities considered;
- many municipalities did not receive funding even though their debt to revenue ratio exceeded 30%;
- many municipalities that did receive funding were left with debt to revenue ratios exceeding 30%;
- many municipalities which received funding are required to increase property, water and sewer, business and poll taxes. In addition, many municipalities which did not receive funding were advised to increase their taxes to improve their debt to revenue ratios. However, the tax rates established by the Department are not consistent and vary by municipality; and
- although the debt relief fund is the responsibility of the Newfoundland Municipal Financing Corporation, the Department entered into agreements with the 13 municipalities for debt relief funding before it was actually approved by the Newfoundland Municipal Financing Corporation.

### 3.35 Debt Relief Program

Figure 2 provides a summary of significant dates and related funding amounts for the 13 municipalities which were allocated funding under the Program, as well as an indication of whether the 30% debt to revenue threshold was met. As noted above, and as Figure 2 shows, both the Town of Harbour Grace and the Town of Flatrock were allocated funding under the Program; however, each had a debt to revenue ratio of less than the 30% targeted under the draft guidelines.

**Figure 2**

#### Debt Relief Program Debt Relief Approval Process 31 March 1999

| Municipality Name       | Financial Review Completed | Agreement Signed | NMFC Approval    | Agreement Amount | Allocated Amount | Debt to Revenue Threshold Met (Yes/No) |
|-------------------------|----------------------------|------------------|------------------|------------------|------------------|----------------------------------------|
| Burnt Islands           | 08 Apr 97                  | 08 Oct 98        | 09 Apr 99        | \$ 194,553       | \$ 258,297       | Yes                                    |
| Fox Cove - Mortier      | N/A                        | 08 Oct 97        | 27 Jan 98        | 358,523          | 233,172          | Yes                                    |
| Harbour Grace           | 25 Sep 97                  | 22 Dec 97        | 27 Jan 98        | 987,195          | 987,195          | No                                     |
| Flatrock                | N/A                        | 19 Dec 97        | 27 Jan 98        | 36,662           | 36,662           | No                                     |
| Humber Arm South        | 19 Nov 97                  | 08 Oct 98        | 09 Apr 99        | 869,197          | 1,140,168        | Yes                                    |
| Norman Cove - Long Cove | 22 Jan 98                  | 31 Mar 98        | 09 Apr 99        | 1,025,000        | 1,024,871        | Yes                                    |
| Campbellton             | 2 Feb 98                   | 08 Oct 98        | 09 Apr 99        | 401,535          | 388,714          | Yes                                    |
| New Perlican            | 25 Mar 98                  | 08 Oct 98        | 09 Apr 99        | 195,025          | 183,307          | Yes                                    |
| Whitby                  | 31 Mar 98                  | 24 Jul 98        | 09 Apr 99        | 230,614          | 260,946          | Yes                                    |
| Summerford              | 16 Jun 98                  | 30 Jun 98        | 09 Apr 99        | 291,242          | 287,420          | Yes                                    |
| Trepassy                | 16 Jun 98                  | 28 May 98        | 29 Jun 99        | 485,000          | 558,793          | Yes                                    |
| Joe Batt's Arm          | 09 Nov 98                  | Not Signed       | Not yet approved | 396,255          | 405,318          | Yes                                    |
| Seldom                  | 16 Nov 98                  | 22 Jul 99        | Not yet approved | 296,670          | 296,670          | Yes                                    |
|                         |                            |                  |                  | \$ 5,767,471     | \$6,061,533      |                                        |





### 3.35 Debt Relief Program

Figure 2 provides a summary of significant dates and related funding amounts for the 13 municipalities which were allocated funding under the Program, as well as an indication of whether the 30% debt to revenue threshold was met. As noted above, and as Figure 2 shows, both the Town of Harbour Grace and the Town of Flatrock were allocated funding under the Program; however, each had a debt to revenue ratio of less than the 30% targeted under the draft guidelines.

**Figure 2**

**Debt Relief Program  
Debt Relief Approval Process  
31 March 1999**

| Municipality Name       | Financial Review Completed | Agreement Signed | NMFC Approval    | Agreement Amount    | Allocated Amount   | Debt to Revenue Threshold Met (Yes/No) |
|-------------------------|----------------------------|------------------|------------------|---------------------|--------------------|----------------------------------------|
| Burnt Islands           | 08 Apr 97                  | 08 Oct 98        | 09 Apr 99        | \$ 194,553          | \$ 258,297         | Yes                                    |
| Fox Cove - Mortier      | N/A                        | 08 Oct 97        | 27 Jan 98        | 358,523             | 233,172            | Yes                                    |
| Harbour Grace           | 25 Sep 97                  | 22 Dec 97        | 27 Jan 98        | 987,195             | 987,195            | No                                     |
| Flatrock                | N/A                        | 19 Dec 97        | 27 Jan 98        | 36,662              | 36,662             | No                                     |
| Humber Arm South        | 19 Nov 97                  | 08 Oct 98        | 09 Apr 99        | 869,197             | 1,140,168          | Yes                                    |
| Norman Cove - Long Cove | 22 Jan 98                  | 31 Mar 98        | 09 Apr 99        | 1,025,000           | 1,024,871          | Yes                                    |
| Campbellton             | 2 Feb 98                   | 08 Oct 98        | 09 Apr 99        | 401,535             | 388,714            | Yes                                    |
| New Perlican            | 25 Mar 98                  | 08 Oct 98        | 09 Apr 99        | 195,025             | 183,307            | Yes                                    |
| Whiteway                | 31 Mar 98                  | 24 Jul 98        | 09 Apr 99        | 230,614             | 260,946            | Yes                                    |
| Summerford              | 16 Jun 98                  | 30 Jun 98        | 09 Apr 99        | 291,242             | 287,420            | Yes                                    |
| Trepassy                | 16 Jun 98                  | 28 May 98        | 29 Jun 99        | 485,000             | 558,793            | Yes                                    |
| Jobbatt's Arm           | 09 Nov 98                  | Not Signed       | Not yet approved | 396,255             | 405,318            | Yes                                    |
| Seldom                  | 16 Nov 98                  | 22 Jul 99        | Not yet approved | 296,670             | 296,670            | Yes                                    |
|                         |                            |                  |                  | <b>\$ 5,767,471</b> | <b>\$6,061,533</b> |                                        |

### 3.35 Debt Relief Program

Our testing also identified two municipalities which had debt outstanding relating to infrastructure which was only partially completed in the past and therefore not servicing the communities, and for which the Department indicated the municipalities had no intention of completing. The Department entered into agreements with these municipalities to pay amounts from the Debt Relief Fund to offset the related NMFC debt. Details relating to each of these municipalities are as follows.

In 1988, funds were approved under the Municipal Capital Works Program for the Town of Flatrock to install a water system, with related debentures totaling \$472,995 being issued. Since then, no further funding has been allocated to the system and it remains a dry line. The Department considered there was no need to complete a detailed financial analysis under the Debt Relief Program as it felt the town was in good financial position. Our review indicated that the debt to revenue ratio was less than 30% and therefore the municipality did not meet the targeted criteria for funding under the Program. However, the Department has agreed to allocate \$36,662 from the Debt Relief Fund to meet the Council's portion of debt installments to the year 2000. In the years 2001 to 2004, the Department is to provide \$36,662 of its annual budget to meet installments that become due. The municipality has agreed not to apply for water and sewer capital funding for a 10-year period. The Department's decision to assume the Council's share of the debt appears to be based on "principle" rather than the financial position of the town as would be expected based on the draft Program guidelines and on the review of other agreements under the Program.

Funding was approved in 1990 under the Municipal Capital Works Program to install a water and sewer system for the Town of Fox Cove-Mortier. This water and sewer system was capped at the entrance of the municipality. Debentures totaling \$455,635 were issued and the town had been required to pay \$47,996 annually on a long term basis. The Department agreed to allocate a total of \$358,523 under the Debt Relief Program to meet arrears on long term debt and installments to the year 2000. In the years 2001 to 2008, the Department is to provide \$47,996 of its annual budget to meet installments that become due. The municipality agreed not to apply for water and sewer capital funding for a 15-year period. There was no detailed financial analysis completed relating to this agreement.

### 3.35 Debt Relief Program

#### (b) Program Agreement Approvals

As noted above, the final debt restructuring allocation at NMFC often differs from the amount included in the agreements signed between the Department and individual municipalities. This is due to such factors as increases in arrears and interest from the time the agreements are signed until final approval and allocation.

In reviewing agreements, it was noted that they were signed by the Department and the municipalities involved prior to receiving approval from the Department of Finance for allocation from the NMFC reserve fund. The Deputy Minister of Finance expressed concerns in this area in a letter to the Deputy Minister of Municipal and Provincial Affairs. The letter states that *"...we have concerns with the process being followed in these circumstances, since the Minister of Finance is required to give final approval with respect to allocations from the Reserve Fund. To enable the Minister to discharge his responsibilities in a timely manner, I am once again requesting that, in the case of municipal refinancings where it is proposed that some portion of payout amounts be covered through the Reserve Fund, the Debt Management Division be informed beforehand so that the prior approval of the Minister may be obtained."*

#### 4. Program Monitoring and Reporting

Our review disclosed that monitoring and reporting mechanisms established to measure success towards achieving Program objectives have not been complied with.

As noted above, the draft guidelines provide that a Debt Relief Program Review Committee was to be in place to ensure the Program objectives are met, issues resolved, progress reviewed, and guidance and direction given. Our review disclosed there were no regular meetings held or minutes kept relating to this Committee. As well, although the Program Manager did prepare some reports on the status of the Program, there was no evidence that reports on the objectives of the Program were required by or presented to the Committee.

We were informed by officials of the Department that the Executive met with the Program Manager on an ad hoc basis. We were further advised that an interdepartmental committee which did exist at the time of our review, had not been established until January 1999. The objective of this committee is to coordinate and maintain an awareness of initiatives with respect to municipal financing issues; however, at the time of our review there were no specific terms of reference approved for the Committee with respect to the Debt Relief Program.

### 3.35 Debt Relief Program

Although not contemplated in the draft guidelines, the Department's Finance Committee has reviewed reports from the Program Manager on municipalities which have been considered and reviewed under the Program; however, the Committee does not regularly review and discuss the Debt Relief Program and again there are no specific terms of reference in place defining its role in relation to the Program.

As well, although the draft guidelines indicated a need to monitor the action plans of the individual municipalities, there was no related monitoring strategy in place.

The draft guidelines also indicate that overview reports would be periodically provided to the Minister of Municipal and Provincial Affairs to inform the House of Assembly, the Newfoundland and Labrador Federation of Municipalities and other stakeholders of the progress of the Debt Relief Program. Our review disclosed that, as at 31 March 1999, there had been no formal report made to the House of Assembly on progress made on the Program objectives as outlined in Figure 1. It was noted that ministerial statements were periodically made on the status of the Program.

#### **Recommendation**

*The Department should ensure that programs developed to address municipal debt issues, such as the Debt Relief Program contain the following elements:*

- *well defined and formally approved program objectives and funding criteria;*
- *approved guidelines defining program objectives, organizational structure, processes, and expected outcomes; and*
- *a process to adequately monitor and report progress towards program objectives.*

#### **Department's Response**

*The Department has revised its Charter and developed Program Guidelines to ensure that the objectives of the Program are met. The main objective of the Program is to analyze the financial position of those municipalities which have been identified as being in financial difficulty. It will focus on negotiating agreements that will restructure their debt, where necessary, and increase taxes to reasonable minimum levels to improve their financial strength and viability as local governments while meeting current operating requirements and debt obligations.*

### 3.35 Debt Relief Program

*The Department recognizes that the Debt Relief Program will not resolve all of the problems of municipal finance and that other initiatives will be required. To achieve strong financial independence, stability and accountability among municipalities will involve a number of strategies. Some strategies will include training of municipal staff and elected officials; innovative ways of providing infrastructure needs; effective accountability mechanisms; a more effective municipal financing framework; and municipal restructuring and sharing of services. The development initiatives that support these strategies will be a challenge for the Department as it endeavors to develop a local government regime that is self sufficient and provides for healthy and safe sustainable communities.*



### **3.36 Municipal Capital Works Program**

#### **Introduction**

The Department of Municipal and Provincial Affairs is responsible for matters relating to local government, municipal financing, assessment, urban and rural planning, development and engineering, and coordination of emergency planning for municipalities.

Municipalities wishing to undertake capital works projects such as water and sewer or road paving must apply to the Department for approval under the Municipal Capital Works Program. Interim financing for approved cost shared projects is generally provided to municipalities by the various chartered banks. After completion of the project, the interim bank debt is then typically refinanced through the Newfoundland Municipal Financing Corporation or, in more recent years, through the chartered banks.

Total approved funding for the 1998-99 Program was \$26.6 million. Individual projects approved will be financed by the Newfoundland Municipal Financing Corporation and chartered banks. Each year, Government provides grants to municipalities to help them pay the principal and interest on this debt.

#### **Scope and Objectives**

We completed our review of the Municipal Capital Works Program in September 1999. Our objectives were to:

- determine the nature and objectives of the Program;
- determine whether Program guidelines were in place and were being complied with;
- review how the Program is administered and how funds are allocated; and
- assess whether monitoring and reporting mechanisms have been established to measure success towards achieving Program objectives.

We were informed that officials at the Department complete the initial ranking of projects to be considered under the Program and make recommendations to the Deputy Minister who, in turn, submits them to the Minister. The Minister, in turn, makes a submission to a Select Committee of Cabinet. Any one of these stakeholders may make changes to the list of projects ranked and recommended; however, reasons for any changes are not always documented in the files. As the list of rankings forms part of a Cabinet submission, the Department declined to provide us with this information. Therefore, we were unable to fully review the systems and processes used in the ranking and selection of capital works projects.



### 3.36 Municipal Capital Works Program

Officials further informed us that the Department has conducted a comprehensive review of the Program; however, we were also unable to obtain the related report as we were informed that it was intended for Cabinet as well.

#### Conclusions

Our review disclosed that:

- Since Cabinet makes the final decision as to which municipal capital works projects are approved for funding by the Province, the information and support for the projects were not made available for my review.
- Our review of the Municipal Capital Works Program indicated that there is no approved, written policy on how the Provincial and municipal cost shared ratios are determined for capital works projects. Prior to 1997, the annual cost sharing arrangements for municipal capital works projects were determined using a formula prescribed in the regulations under the *Municipal Grants Act*. These regulations were discontinued in 1996 with the intention that the formula for funding be replaced by departmental policy. This was never done.
- Departmental officials informed us that the cost shared ratios depend on the municipality's debt to revenue ratio. However, in 14 of the 20 projects reviewed, the approved cost shared ratio was not consistent with the ratio which would be expected using the criteria indicated by the Department.
- The Department has completed its strategic plan and is currently in the process of developing operational plans for its divisions. Although officials did inform us that policies and procedures relating to the Municipal Capital Works Program are being developed, there was no indication that the calculation of cost sharing ratios would be consistently applied and based on a prescribed formula.

#### Findings and Recommendations

##### 1. Municipal Capital Works Program

Municipalities wishing to cost share capital works projects such as water and sewer or road paving with the Province must apply to the Department of Municipal and Provincial Affairs for approval. Interim financing for approved cost shared projects is generally provided to municipalities by chartered banks. After completion of the project, the bank loan is then refinanced either through the Newfoundland Municipal Financing

### 3.36 Municipal Capital Works Program

Corporation or, in more recent years, through a chartered bank. To assist municipalities in repaying these loans, the Department provides annual grants for its share of principal and interest costs. In 1998-99, total funding approved by Government for the Municipal Capital Works Program was \$26.6 million. The debt associated with projects funded through the Program will be repaid by the municipalities and the Department of Municipal and Provincial Affairs. Road related projects are typically financed over a 10 year period while water and sewer projects are typically financed over a 15 year period. For 1998-99 the Department paid \$28.5 million in interest payments and \$38.3 million in principal repayments for the debt related to capital works projects from prior years.

As noted in the Scope and Objectives section of this report item, we were unable to fully audit the systems and processes used in the ranking and selection of capital works projects. This was due to the Department declining to provide us with the final list of projects ranked and recommended by the Department and the reasons for any changes made to these rankings during the final approval process. Presently, the *Auditor General Act* does not permit the Auditor General access to information that contains recommendations submitted by a Minister of the Crown to the Executive Council or the background analysis.

## 2. Program Administration and Funding Allocation

### (a) Program Criteria

Prior to 1997, the annual cost sharing arrangements between the Province and municipalities for water and sewer capital works projects were determined using a formula prescribed in the regulations under the *Municipal Grants Act*. These regulations were discontinued in 1996 as a result of Government's Regulatory Reform Process with the intention that the formula for funding provided for under the regulations would be replaced by departmental policy. For road work prior to 1997, the Province paid 60% of the financing cost while the municipalities paid 40%.

Our review of the Municipal Capital Works Program indicated that there is no approved, written policy on how the Provincial and municipal cost shared ratios are determined for capital works projects.

Since there is no approved written policy on how the cost shared ratios are determined, Departmental officials informed us that cost shared ratios are calculated for each capital works project in accordance with informal criteria but are subject to change throughout the approval process. The criteria which officials provided to us are outlined in Figure 1.

### 3.36 Municipal Capital Works Program

Figure 1

**Municipal Capital Works Program  
Cost Sharing Ratio Criteria  
(Provincial/Municipal)**

| Type of Project | Debt to Revenue Ratio of Municipality | Cost Shared Ratio (Provincial/Municipal) |
|-----------------|---------------------------------------|------------------------------------------|
| Water and Sewer | Less than 40%                         | 50 / 50                                  |
|                 | 40% to 50%                            | 75 / 25                                  |
|                 | Greater than 50%                      | 100 / 0                                  |
| Roads           | Less than 40%                         | 25 / 75                                  |
|                 | 40% to 50%                            | 50 / 50                                  |
|                 | Greater than 50%                      | 75 / 25                                  |

Source: Departmental information

**(b) Program Testing**

The Department provided a listing relating to individual projects approved under the Program for the 1998-99 fiscal year. The listing included 237 projects approved for 136 municipalities at a cost of \$25.4 million. Figure 2 provides a summary of the 10 municipalities with the highest funding approved. As indicated in the figure, these 10 municipalities were awarded \$13.8 million or 54% of the total \$25.4 million in project funding. Included in these 10 municipalities were two of the Province's three cities, which were awarded a total of \$8.0 million.

### 3.36 Municipal Capital Works Program

**Figure 2**

**Project Funding  
Municipalities with Highest Funding Approved  
Year Ended 31 March 1999**

| <b>Municipality</b>  | <b>Number of Projects<br/>Approved</b> | <b>Total Funding<br/>Approved</b> |
|----------------------|----------------------------------------|-----------------------------------|
| St. John's           | 9                                      | \$ 5,258,500                      |
| Corner Brook         | 5                                      | 2,721,000                         |
| Old Perlican         | 1                                      | 1,729,000                         |
| Conception Bay South | 2                                      | 830,000                           |
| Hermitage-Sandyville | 2                                      | 645,500                           |
| New-Wes-Valley       | 7                                      | 572,550                           |
| Twillingate          | 4                                      | 566,000                           |
| Clareville           | 4                                      | 506,250                           |
| Deer Lake            | 3                                      | 465,000                           |
| Carbonear            | 6                                      | 456,327                           |
|                      |                                        | \$ 13,750,127                     |

We selected 20 capital works projects to determine whether the cost sharing ratios were in accordance with the criteria indicated in Figure 1 as provided by Departmental officials and compared these ratios to the final approved cost sharing ratios. Our testing indicated that 14 of the 20 projects were cost shared using a ratio that was not consistent with the criteria provided. Figure 3 provides details of funding approved for these 14 projects.

### 3.36 Municipal Capital Works Program

Figure 3

**Project Funding  
Cost Shared Ratios  
(Provincial/Municipal)**

| Municipality      | Project Type              | Project Cost | Debt/<br>Revenue Ratio | Cost Shared<br>Ratio per<br>Criteria | Approved<br>Cost Shared<br>Ratio<br>(Provincial/Municipal) |
|-------------------|---------------------------|--------------|------------------------|--------------------------------------|------------------------------------------------------------|
| Carbonear         | Paving and Road Upgrading | \$ 60,000    | 23.7                   | 25 / 75                              | 100 / 0                                                    |
| Cornier Brook     | Paving and Road Upgrading | 1,600,000    | 18.8                   | 25 / 75                              | 100 / 0                                                    |
| Frenchman's Cove  | Paving and Road Upgrading | 60,114       | 40.6                   | 50 / 50                              | 25 / 75                                                    |
| Harbour Grace     | Paving and Road Upgrading | 32,000       | 27.3                   | 25 / 75                              | 100 / 0                                                    |
| Harbour Grace     | Paving and Road Upgrading | 80,000       | 27.3                   | 25 / 75                              | 50 / 50                                                    |
| Mount Pearl       | Paving and Road Upgrading | 104,000      | 19.5                   | 25 / 75                              | 50 / 50                                                    |
| New-Wes-Valley    | Water and Sewer           | 220,000      | 32.7                   | 50 / 50                              | 100 / 0                                                    |
| Old Perlican      | Water and Sewer           | 1,729,000    | 38.2                   | 50 / 50                              | 100 / 0                                                    |
| Pouch Cove        | Paving and Road Upgrading | 95,703       | 48.1                   | 50 / 50                              | 25 / 75                                                    |
| St. Lawrence      | Water and Sewer           | 346,000      | 30.7                   | 50 / 50                              | 65 / 35                                                    |
| Summerford        | Water and Sewer           | 189,000      | 49.9                   | 75 / 25                              | 100 / 0                                                    |
| Upper Island Cove | Water and Sewer           | 372,000      | 27.6                   | 50 / 50                              | 75 / 25                                                    |
| Victoria          | Water and Sewer           | 65,380       | 44.1                   | 75 / 25                              | 100 / 0                                                    |
| Whiteway          | Water and Sewer           | 70,000       | 47.7                   | 75 / 25                              | 100 / 0                                                    |

Source: Departmental information



### **3.36 Municipal Capital Works Program**

In the case of Frenchman's Cove, discussion with Department officials indicated that the difference in cost sharing ratio was caused by a computational error and the actual cost sharing ratio should have been as provided for in the criteria. In the case of Pouch Cove, we were advised that the difference in cost sharing ratios was caused by the use of a debt to revenue ratio that, due to the lateness of the project approval, may not have been accurate. In the other cases, Department officials indicated a variety of reasons for the differences in approved cost sharing ratios compared to those expected based on the criteria, including: the impact of transferring industrial water systems to the municipalities; the negative impact of additional debt for those municipalities which had been allocated funding under the Department's Debt Relief Funding Program; and discussions between the Department and the municipalities involved as to the municipalities' responsibility or ability to repay related debt.

### **3. Program Monitoring and Reporting**

The Municipal Capital Works Program is a major Government program. In 1998-99, Government approved \$26.6 million in funding for the Program. In addition, Government provided grants totalling \$28.5 million and \$38.3 million to pay interest charges and principal debt repayments respectively relating to municipal capital works programs approved in previous years. Given the significant cost of this program there should be regular reporting on the objectives and accomplishments of this program. Our review disclosed that there is no regular reporting on this program.

The Department has developed a strategic plan and is currently in the process of completing operational plans for its divisions. As a result, approved guidelines defining program objectives, organizational structure, processes, and expected outcomes were not in place for the Municipal Capital Works Program. Although officials did inform us that policies and procedures relating to the Municipal Capital Works Program are being developed, there was no indication that the calculation of cost sharing ratios would be consistently applied based on a prescribed formula.

In addition, the Department has not established a process to adequately monitor and report on the program's achievements.



### **3.36 Municipal Capital Works Program**

#### **Recommendations**

*The Department should establish a formula that would ensure that municipal capital works cost sharing ratios are determined in an equitable manner and be transparent.*

*As a result of our finding inconsistencies in the cost sharing ratios for 14 of 20 municipal capital works projects reviewed, the Department should review existing cost sharing ratios to ensure they are consistently applied.*

*The Department should continue with its strategic planning process.*

*The Department should report annually to the House of Assembly on the programs which it delivers including the Municipal Capital Works Program.*

#### **Department's Response**

*For the 1999/2000 fiscal year, the Department has established a 50/50 Provincial/Municipal cost sharing ratio. This formula is applied consistently with the exception of demonstrated emergency projects, whose councils have maximized their tax rates to meet the minimum requirement for debt relief.*

*There is now no legislative requirement for Departments to table their annual reports in the House of Assembly. If such a requirement is set as policy by Government, the Department will be well positioned to present the reports as a result of recent strategic planning initiatives.*

### 3.37 Job Creation Program

#### Introduction

During the fiscal years ended 31 March 1998 and 1999, Cabinet approved funding of \$18.1 million for a special employment initiative known as the Job Creation Program. The purpose of this Program was to create short-term employment throughout the Province. The Program was administered by the following four departments: Municipal and Provincial Affairs, Works, Services and Transportation, Forest Resources and Agrifoods, and Human Resources and Employment. Figure 1 provides information on the approved funding allocated to each of these departments.

Funding for the Job Creation Program was not part of the original approved budget for these departments. Instead, as shown in Figure 2, \$9 million was provided from the Province's Contingency Fund, \$2.6 million was provided through a Special Warrant, and \$6.5 million was transferred from other Government programs.

**Figure 1**

**Total Approved Job Creation Funding  
31 March  
(\$Millions)**

| Department                         | 1998          | 1999         | Total         |
|------------------------------------|---------------|--------------|---------------|
| Municipal and Provincial Affairs   | \$6.1         | \$5.0        | \$11.1        |
| Forest Resources and Agrifoods     | 3.0           | 1.5          | 4.5           |
| Works, Services and Transportation | 1.2           | 1.0          | 2.2           |
| Human Resources and Employment     | 0.3           | -            | 0.3           |
| <b>Total</b>                       | <b>\$10.6</b> | <b>\$7.5</b> | <b>\$18.1</b> |

Source: Government's accounting records

### 3.37 Job Creation Program

Figure 2

**Sources of Funding  
Job Creation Program  
31 March  
(\$Millions)**

| Fiscal Year | Source of Funding             | Municipal and Provincial Affairs | Forest Resources and Agrifoods | Works, Services and Transportation | Human Resources and Employment | Total       |
|-------------|-------------------------------|----------------------------------|--------------------------------|------------------------------------|--------------------------------|-------------|
| 1998        | Contingency Fund              | 1.0                              | 2.5                            | .7                                 | .3                             | 4.5         |
|             | Special Warrant               | 2.6                              | -                              | -                                  | -                              | 2.6         |
|             | Transfers From Other Programs | 2.5                              | .5                             | .5                                 | -                              | 3.5         |
|             | Sub-Total                     | 6.1                              | 3.0                            | 1.2                                | 0.3                            | 10.6        |
| 1999        | Contingency Fund              | 3.0                              | 1.0                            | .5                                 | -                              | 4.5         |
|             | Transfers From Other Programs | 2.0                              | .5                             | .5                                 | -                              | 3.0         |
|             | Sub-Total                     | 5.0                              | 1.5                            | 1.0                                | -                              | 7.5         |
|             | <b>Total</b>                  | <b>11.1</b>                      | <b>4.5</b>                     | <b>2.2</b>                         | <b>0.3</b>                     | <b>18.1</b> |

Source: Government's accounting records

To coordinate the implementation of the 1998-99 Job Creation Program, Cabinet established a Review Committee. This Committee consisted of the Minister of Municipal and Provincial Affairs, the Minister of Forest Resources and Agrifoods, the Minister of Works, Services and Transportation, a Member of the House of Assembly, and officials of the Department of Municipal and Provincial Affairs. The Committee was responsible for coordinating the implementation of the Job Creation Program, including all project approvals.

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Source: Government's accounting records

### 3.37 Job Creation Program

**Figure 2**

**Sources of Funding  
Job Creation Program  
31 March  
(\$Millions)**

| <b>Fiscal Year</b> | <b>Source of Funding</b>      | <b>Municipal and Provincial Affairs</b> | <b>Forest Resources and Agrifoods</b> | <b>Works, Services and Transportation</b> | <b>Human Resources and Employment</b> | <b>Total</b> |
|--------------------|-------------------------------|-----------------------------------------|---------------------------------------|-------------------------------------------|---------------------------------------|--------------|
| 1998               | Contingency Fund              | 1.0                                     | 2.5                                   | .7                                        | .3                                    | 4.5          |
|                    | Special Warrant               | 2.6                                     | -                                     | -                                         | -                                     | 2.6          |
|                    | Transfers From Other Programs | 2.5                                     | .5                                    | .5                                        | -                                     | 3.5          |
|                    | <b>Sub-Total</b>              | <b>6.1</b>                              | <b>3.0</b>                            | <b>1.2</b>                                | <b>0.3</b>                            | <b>10.6</b>  |
| 1999               | Contingency Fund              | 3.0                                     | 1.0                                   | .5                                        | -                                     | 4.5          |
|                    | Transfers From Other Programs | 2.0                                     | .5                                    | .5                                        | -                                     | 3.0          |
|                    | <b>Sub-Total</b>              | <b>5.0</b>                              | <b>1.5</b>                            | <b>1.0</b>                                | <b>-</b>                              | <b>7.5</b>   |
|                    | <b>Total</b>                  | <b>11.1</b>                             | <b>4.5</b>                            | <b>2.2</b>                                | <b>0.3</b>                            | <b>18.1</b>  |

Source: Government's accounting records

To coordinate the implementation of the 1998-99 Job Creation Program, Cabinet established a Review Committee. This Committee consisted of the Minister of Municipal and Provincial Affairs, the Minister of Forest Resources and Agrifoods, the Minister of Works, Services and Transportation, a Member of the House of Assembly, and officials of the Department of Municipal and Provincial Affairs. The Committee was responsible for coordinating the implementation of the Job Creation Program, including all project approvals.





### 3.37 Job Creation Program

As the Department of Municipal and Provincial Affairs was allocated \$11.1 million or 61% of the total approved funding of \$18.1 million, we limited our review of the Job Creation Program to this Department. Total funding of \$11.1 million allocated to this Department was approved by Cabinet under five separate Job Creation programs throughout the years ended 31 March 1998 and 1999. Figure 3 provides information on available funding, actual expenditures and the number of applications approved for each of these five programs.

The Review Committee at the Department of Municipal and Provincial Affairs consisted of the Minister of Municipal and Provincial Affairs and three Members of the House of Assembly. In addition, the Department assigned one of its staff as Job Creation Coordinator.

Figure 3

**Department of Municipal and Provincial Affairs**  
**Summary of Funding, Expenditure and Applications**  
**Job Creation Program**  
**31 March**

| Fiscal Year  | Program  | Amount Authorized   | Total Approved Projects | Total Project Expenditures | Number of Applications | Deadline for Applications |
|--------------|----------|---------------------|-------------------------|----------------------------|------------------------|---------------------------|
| 1998         | 1        | \$1,000,000         | \$999,080               | \$999,080                  | 177                    | 31 July 1997              |
|              | 2        | 1,000,000           | 1,000,907               | 1,000,907                  | 148                    | 5 December 1997           |
|              | 3        | 4,100,000           | 4,092,752               | 4,092,722                  | 492                    | 23 January 1998           |
|              | Subtotal | \$6,100,000         | \$6,092,739             | \$6,092,709                | 817                    |                           |
| 1999         | 4        | \$500,000           | \$346,129               | \$346,129                  | 35                     | 7 December 1998           |
|              | 5        | 4,500,000           | 4,550,043               | 4,550,043                  | 602                    | 25 January 1999           |
|              | Subtotal | \$5,000,000         | \$4,896,172             | \$4,896,172                | 637                    |                           |
| <b>TOTAL</b> |          | <b>\$11,100,000</b> | <b>\$10,988,911</b>     | <b>\$10,988,881</b>        | <b>1,454</b>           |                           |

Source: Department of Municipal and Provincial Affairs

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|--------------------|----------------|--------------------------|--------------------------------|-----------------------------------|-------------------------------|----------------------------------|
| 1998               | 1              | \$1,000,000              | \$999,080                      | \$999,080                         | 177                           | 31 July 1997                     |
|                    | 2              | 1,000,000                | 1,000,907                      | 1,000,907                         | 148                           | 5 December 1997                  |
|                    | 3              | 4,100,000                | 4,092,752                      | 4,092,722                         | 492                           | 23 January 1998                  |
|                    | Subtotal       | \$6,100,000              | \$6,092,739                    | \$6,092,709                       | 817                           |                                  |
| 1999               | 4              | \$500,000                | \$346,129                      | \$346,129                         | 35                            | 7 December 1998                  |
|                    | 5              | 4,500,000                | 4,550,043                      | 4,550,043                         | 602                           | 25 January 1999                  |
|                    | Subtotal       | \$5,000,000              | \$4,896,172                    | \$4,896,172                       | 637                           |                                  |
| <b>TOTAL</b>       |                | <b>\$11,100,000</b>      | <b>\$10,988,911</b>            | <b>\$10,988,881</b>               | <b>1,454</b>                  |                                  |

Source: Department of Municipal and Provincial Affairs

### **3.37 Job Creation Program**

Departmental officials informed us that the Departmental Review Committee established the following program objectives:

- to provide a short term employment response program;
- to support labour intensive job creation initiatives;
- to address the most pressing needs for families and others with no source of employment income;
- to focus on areas of high unemployment where needs are most warranted; and
- to leverage and combine with other programs and fundraising initiatives to supply materials and other non-labour related project components.

Departmental officials also informed us that:

- of the total approved funding of \$11 million, this Review Committee allocated \$10.5 million to the 48 electoral districts as indicated in Figure 4;
- the Job Creation Program was not publicly advertised;
- it was incumbent upon each Member of the House of Assembly to advise interested project sponsors of available program funding; and
- all applications for funding within an electoral district are reviewed and approved by that district's Member of the House of Assembly. These applications are then forwarded to the Departmental Review Committee to ensure projects meet Program eligibility criteria.

At the time of our audit in October 1999, Cabinet had approved an additional \$5 million in funding for another Job Creation Program of which \$3.5 million and \$1.5 million is to be administered by the Department of Municipal and Provincial Affairs and the Department of Works, Services and Transportation respectively. The deadline for applications for this additional funding is scheduled for 10 December 1999.

#### **Scope and Objectives**

In October 1999, we commenced a review of the Job Creation Program in the Department of Municipal and Provincial Affairs. The objective of this review was to determine whether adequate policies and procedures exist to ensure the Department properly administered the Program.

### 3.37 Job Creation Program

There were 1,454 applications totalling \$11 million approved for the Job Creation Program of the Department of Municipal and Provincial Affairs in 1997-98 and 1998-99.

We examined files for 56 approved applications with total approved funding of \$833,416. We also selected a sample of 14 applications that had been rejected for funding to determine whether there was adequate documentation to support the reasons for rejection. Our review covered the period of 1 April 1997 to 31 March 1999.

#### Conclusions

The Department's administration of the Job Creation Program is not adequate. In particular:

- Project files lacked adequate documentation to support funding decisions and we were often unable to determine if approved applications met established eligibility and selection criteria.
- Additional funding was advanced to project sponsors without project applications being completed and without adequate documentation on how previously approved funds had been spent and how the additional funding is intended to be spent.
- In contravention of the *Financial Administration Act*, the Department made payments for the Job Creation Program from funds approved by the House of Assembly for Special Assistance to municipalities.
- Although project sponsors are required to submit a financial report supporting total project expenditures before the final 25% funding installment is paid by the Department, these funds have often been paid to the sponsor groups prior to the receipt of any financial reports. In general, financial reports were not received by the Department on a timely basis.
- The Department is not receiving adequate information from project sponsors to ensure that program guidelines were followed and that project funding was used for its intended purpose. For example, documentation to adequately support project expenditures in the form of invoices for materials and payroll records for salaries are generally not provided to the Department.

### 3.37 Job Creation Program

Ministers of the Crown are responsible for policy development and it is the responsibility of public servants to implement these policies and deliver the Government programs which reflect these policies. I am concerned about the manner in which the Job Creation Program is being delivered. For example, the Program was not publicly advertised and made available to all residents of the Province, funding for the Program has been allocated based on electoral district rather than the merit of applications or other objective assessment, and applications are not subjected to a consistent and rigorous review and evaluation prior to being approved.

#### Findings and Recommendations

##### Review and Approval of Applications

Adequate policies and procedures are necessary to ensure that approved applications are those most likely to achieve program objectives. This would include reviewing the applications to ensure established eligibility and selection criteria are met and adequately documenting the resulting assessment decisions.

Job Creation Program guidelines indicate that eligible sponsors who receive program funding are to include non-profit organizations, community based agencies, service groups, churches, municipal councils, local service district committees and development agencies. The types of projects funded under the Job Creation Program are required to meet the following criteria:

- relatively short term;
- small-scale;
- capable of immediate start-up once funding has been approved; and
- labour intensive with a labour component of at least 70% ie overhead/materials cannot exceed 30% of the total project cost.

Program Guidelines indicated that projects with the highest labour content were to be given preference under this program.

We were informed that sponsor groups seeking funding under the Job Creation program were required to submit an application which was usually reviewed by the applicable Member of the House of Assembly, the Job Creation Coordinator and the Review Committee.

Figure 4 indicates allocation of \$10.5 of the \$11.0 million approved funding to the 48 electoral districts.



### 3.37 Job Creation Program

Figure 4

#### Funding by Electoral District

| Electoral District            | Approved Funding Amount |
|-------------------------------|-------------------------|
| Cartwright-L'anse au Clair    | \$ 387,045              |
| Carbonear-Harbour Grace       | 378,250                 |
| Placentia & St. Mary's        | 335,388                 |
| Twillingate & Fogo            | 298,084                 |
| The Straits & White Bay North | 294,986                 |
| St. Barbe                     | 290,107                 |
| Port De Grave                 | 285,000                 |
| Bonavista North               | 284,827                 |
| Humber West                   | 265,205                 |
| Port Au Port                  | 264,153                 |
| Exploits                      | 262,220                 |
| Grand Bank                    | 258,748                 |
| Fortune Bay-Cape La Hune      | 244,637                 |
| Burgeo & Lapoile              | 242,802                 |
| Humber East                   | 241,871                 |
| Bay of Islands                | 241,237                 |
| Burin-Placentia West          | 240,360                 |
| Bellevue                      | 239,304                 |
| Ferryland                     | 239,033                 |
| Grand Falls-Buchans           | 238,238                 |
| Bonavista South               | 227,190                 |



### 3.37 Job Creation Program

Figure 4 (cont.)

| Electoral District                | Approved Funding Amount |
|-----------------------------------|-------------------------|
| Humber Valley                     | 223,473                 |
| St. John's Centre                 | 223,344                 |
| Harbour Main-Whitbourne           | 218,028                 |
| Gander                            | 216,618                 |
| Terra Nova                        | 214,331                 |
| Trinity-Bay De Verde              | 210,406                 |
| Torngat Mountains                 | 208,705                 |
| Labrador West                     | 204,705                 |
| Lake Melville                     | 202,057                 |
| Topsail                           | 201,860                 |
| Lewisporte                        | 199,236                 |
| Trinity North                     | 198,145                 |
| St. George's-Stephenville East    | 190,023                 |
| Conception Bay East & Bell Island | 189,223                 |
| Baie Verte                        | 173,189                 |
| St. John's North                  | 170,517                 |
| Windsor-Springdale                | 159,553                 |
| Cape St. Francis                  | 151,002                 |
| Kilbride                          | 140,428                 |
| Mount Pearl                       | 139,964                 |
| Conception Bay South              | 134,751                 |
| Signal Hill-Quidi Vidi            | 127,619                 |

### 3.37 Job Creation Program

Figure 4 (cont.)

| Electoral District                                                                           | Approved Funding Amount |
|----------------------------------------------------------------------------------------------|-------------------------|
| Virginia Waters                                                                              | 121,258                 |
| St. John's South                                                                             | 110,549                 |
| St. John's West                                                                              | 110,000                 |
| Waterford Valley                                                                             | 106,000                 |
| St. John's East                                                                              | 105,089                 |
| St. John's MHA's                                                                             | 80,153                  |
| <b>Sub-Total - Allocated to electoral districts</b>                                          | <b>10,488,911</b>       |
| Allocated to the Department of Works, Services and Transportation for brush cutting projects | 500,000                 |
| <b>TOTAL</b>                                                                                 | <b>\$10,988,911</b>     |

Source: Department of Municipal and Provincial Affairs

Our review of this area indicated the following:

- Although a formal letter is sent to all successful applicants by the Minister of Municipal and Provincial Affairs indicating approval of funding, decisions of the Departmental Review Committee are not formally documented. Discussions with the Program Coordinator indicate that the project approval process is very informal. There are no formal meetings of the Departmental Review Committee, rather the Coordinator obtains verbal approval from one or more of the Committee members to fund the project. As a result of inadequate documentation, we were unable to determine rationale for funding decisions and whether the Departmental Review Committee had approved projects for program funding.

### 3.37 Job Creation Program

- Application guidelines indicate that projects that have the highest labour content will be given preference under this Program. The Departmental Review Committee does not, however, wait until the application deadline to assess all applications together but allocates funding as applications are received. This process does not facilitate a comparison of all applications to each other for the purposes of determining which projects have the highest labour content and thus would contribute more to the program objective of creating short-term employment. In addition, a review of a sample of rejected applications indicated that this process has resulted in certain sponsor groups not receiving funding because available funding had already been committed; however, these sponsor groups had submitted applications prior to the required application deadline.
- For the 56 projects reviewed, 4 sponsor groups who had already received funding of \$54,775 under the program, received additional funding of \$26,000 without completing new applications. In these cases, the sponsor group submitted a letter requesting additional funds but the letters did not contain sufficient information to determine how the additional funding was intended to be spent. In addition, at the time of the request for additional funding, the Department had not received any support for project expenditures already incurred through previous approved funding.
- For another project reviewed which was originally approved on 27 January 1998 for \$75,000, additional funding of \$150,000 was advanced on six separate occasions over a period of a year and a half without applications always being submitted. When applications were not completed, the sponsor group had submitted a letter to the Department requesting additional funding; however, again these letters did not provide sufficient information to determine how this additional funding was going to be spent nor had the Department received any support for project expenditures already incurred. A financial report to support the \$225,000 was not received until 24 November 1998 and identified a funding deficit of \$12,300. The Department paid an additional \$15,000 to this group in November 1998.

Additional funding totalling \$103,000 was advanced to this sponsor group on four separate occasions between January and March 1999 without any applications being completed. Again, although letters from the sponsor groups requesting the funding were on file, the letters did not contain sufficient information to determine how the additional funding was intended to be spent. The financial report containing information on expenditures

### 3.37 Job Creation Program

totalling \$103,000 incurred by the sponsor group was not received by the Department until 31 August 1999 and identified a funding deficit of \$2,700. In addition, as this sponsor group received additional funding for project continuation over a two year period it did not meet the Program guidelines of being relatively short-term.

- Application files often did not contain sufficient information to determine if the project met the selection criteria with respect to being short-term, small-scale, capable of immediate start-up and labour intensive (i.e. greater than 70%). For example, the project descriptions were either not provided or were very vague indicating that it was for "work around the community" or "maintenance to Town infrastructure".
- As Members of the House of Assembly approve applications, there may be instances where applications are not forwarded to the Department. A review of rejected applications which were available indicated that, in general, application content and scope were of a similar nature to those projects approved for funding; however, reasons for funding rejection were not well documented. When reasons were documented it was usually attributed to available funding having already been committed.

#### Payments Without Authority

Of the projects selected for review, we found four cheques totalling \$67,500 which were paid to two sponsor groups prior to the approval of the Program by Cabinet.

Cabinet approved funding of \$500,000 on 17 November 1998 and \$4.5 million on 25 January 1999 for the 1998-99 Job Creation Program. Our review of selected projects determined that for two projects a total of \$67,500 had been paid to the project sponsors between 4 August and 10 November 1998, before the Program and its funding was approved by Cabinet.

The payments were made from the Department's Special Assistance Program which is supposed to be used for special funding to municipalities. There was no authority to make payments for the Job Creation Program from funds approved by the House of Assembly for Special Assistance to municipalities. As a result, the payments totalling \$67,500 were made in contravention of the *Financial Administration Act*.

### **3.37 Job Creation Program**

#### **Project Monitoring**

Effective monitoring of projects is essential to ensure that program objectives are being achieved, program guidelines are being adhered to and funds are being spent for their intended purpose. Our review of this area indicated that, in general, the Department is not receiving adequate information from the project sponsor to determine whether program guidelines are being followed and funds are being spent as approved. In particular:

- Program guidelines require that to qualify for employment under this program, a person must have an attachment to the labour force, is unemployed and is not in receipt of benefits under the Atlantic Groundfish Strategy or is retired on an old age, CPP or other public or private pension plan. Although the Department receives a list of names and social insurance numbers of individuals hired for a project from the sponsor group, the Department does not perform any verification procedures to ensure that these individuals actually qualified for employment as specified in the guidelines.
- Funding for approved projects occur in two installments: 75% upon approval of the application and 25% upon completion of the project and receipt by the Department of a financial report together with all invoices for materials and payroll information. This process helps ensure that financial and other project information is received by the Department on a timely basis and also allows the Department to withhold the remaining 25% if the project funding was not spent as intended. In one project reviewed, 100% of the funding in the amount of \$15,000 was advanced upon approval of the application. In the majority of other projects reviewed, the final 25% installment was paid to the sponsor group prior to the receipt of the financial reports by the Department. In general, financial reports were not received by the Department on a timely basis.
- At the end of our review in October of 1999, there were three projects for which the financial report was not submitted even though 100% of the approved funding had been disbursed. These reports were all required to be submitted prior to 31 March 1999. As a result, the Department has not been able to substantiate the validity of project expenditures for these three projects. For all other projects reviewed, although financial reports had been submitted by the sponsor groups, the reports often lacked adequate information to verify project expenditures. For example:



### 3.37 Job Creation Program

- in some cases invoices for materials were provided but the invoices did not indicate the nature of the item purchased;
  - in some cases a listing of the nature of the materials was provided but supporting invoices were not included; and
  - in one project, although a listing of employees and the amount they were paid was provided, there was no support provided in the form of payroll journals, record of employment or cancelled cheques to substantiate the payroll amounts.
- Program guidelines require that the labour rate paid by project sponsors be limited to the Province's minimum wage, unless a different rate is approved by the Review Committee. In reviewing the financial reports submitted by the project sponsors, a number of instances were noted where the sponsor paid employees in excess of the Province's minimum wage and no documentation was on file to indicate that the Review Committee had approved this increased wage rate.

For all other financial reports reviewed where payroll was applicable (payroll component for some projects was funded by the Federal government), files did not contain sufficient information to determine if the labour rate paid was limited to the Province's minimum wage.

- Project guidelines require that projects be completed by 31 March of the year in which the project was approved. The guidelines also indicate that no payment will occur after that date and that failure to complete projects by this deadline will result in the balance of funding (25%) being cancelled. Our review indicated that five projects that received funding of \$238,940 were not completed by 31 March in the year in which they were approved but the balance of funding was issued to the project sponsor.

#### **Recommendations**

*Decisions relating to project approvals and rationale for funding decisions should be formally documented.*

*To facilitate selecting projects that have the highest labour component, the Department should review the process of allocating funding before all applications have been received.*



### **3.37 Job Creation Program**

*The Department should ensure that all projects approved for funding have a completed application on file that contains sufficient information to indicate that projects meet the established selection criteria.*

*The Department should ensure that payments to sponsor groups are paid out of approved program funding.*

*Prior to issuing the final 25% instalment of funding, the Department should ensure that the project sponsor submits a financial report. This report should be reviewed to ensure that it contains adequate support for project expenditures and that the project sponsor has complied with all program guidelines.*

#### **Department's Response**

*As recommended by the Auditor General, the Department will, in the future, endeavour to document decisions relating to project approvals as well as the rationale for these funding decisions.*

*The Job Creation Programs which the Department has administered since 1996 have been announced and funded during the fiscal year. Given the nature of this Program, it would not be practical to predetermine and rank applications. This would result in excessive administrative burden and delays in project approvals. The Department will, however, review its approval/evaluation process with a view to potential improvements in approval of priority projects.*

*In future, the Department will endeavour to ensure that all approved projects have a properly completed application on file.*

*In those instances where the Auditor General has noted that payments from other funding areas occurred early in the initial program while waiting for the processing of funding allocations for the Job Creation Programs, it was deemed that this action was necessary in order to get several projects started as early as possible. The only option available at the time in order to get these projects started was to use funding from within existing allocations. The plan was to then replenish the other fund from Job Creation dollars. Such occurrences did not happen subsequent to funding being allocated for the Program. The instances noted would have been exceptions.*

### **3.37 Job Creation Program**

*Based on final results from the projects, the Department may need to review and revise the guidelines as they refer to advancing the funds. The guidelines presently state that the final 25% of the project cost will only be paid on the basis of a final report. From a practical perspective, this often results in a "chicken or egg" situation, with the 25% funding being required to complete the project and finish the final report. The Department will review the accountability section of its guidelines and make recommendations for changes.*

### 3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement

#### Introduction

Of the \$100 million approved under the Canada-Newfoundland Economic Renewal Agreement (ERA) in June 1996, \$22.85 million was allocated to the Tourism Program. This was subsequently increased to \$26.85 million which has been allocated among various projects as indicated in Figure 1. As of 31 March 1999, of the \$26.85 million allocated to the Tourism program, \$20.95 million had been spent.

Figure 1

#### ERA Tourism Funding By Project \$ Million

| Project Name                                                   | Original Project Allocation | Revised Project Allocation | Expenditures 31 March 1999 |
|----------------------------------------------------------------|-----------------------------|----------------------------|----------------------------|
| Interpretation Facilities (9 Projects)                         | \$10.55                     | \$10.53                    | \$9.97                     |
| 1997 Events Support (3 Projects)                               | 2.50                        | 2.56                       | 2.56                       |
| Marketing                                                      | 3.80                        | 3.83                       | 3.64                       |
| Reservation System                                             | 1.00                        | 1.00                       | .97                        |
| Cultural Industry Initiatives (Application Driven)             | 2.50                        | 2.50                       | 2.34                       |
| Marketing Newfoundland as a Film, Video and Audio Location     | 1.00                        | *                          | -                          |
| T'Railway Linear Park                                          | .50                         | .50                        | .50                        |
| Living Interpretations (Application Driven)                    | 1.00                        | .93                        | .62                        |
| Blomidon Golf & Country Club                                   | -                           | .90                        | .25                        |
| Humber Valley Visitors and Convention Bureau (Marble Mountain) | -                           | .10                        | .10                        |
| St. John's Civic Centre Corporation                            | -                           | 4.00                       | -                          |
| <b>Total</b>                                                   | <b>\$22.85</b>              | <b>\$26.85</b>             | <b>\$20.95</b>             |

Source: Original and revised Schedule "B" of the ERA and the 31 March 1999 ERA Financial Summary Worksheet

\* This initiative was reallocated to the Advanced Technology Program.



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### 3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement

The administration and management of the Agreement is the responsibility of the Management Committee which consists of a Federal and Provincial co-chair who are jointly appointed by the Federal and Provincial governments. For each program area, the Management Committee has established Implementation Committees to which it has delegated many of its responsibilities under the Agreement. All projects are administered by either the Federal or Provincial government. Provincially administered tourism projects are managed either directly by the Department of Tourism, Culture and Recreation or by a third party contracted by the Department.

#### Scope and Objectives

We reviewed 9 selected projects totaling \$7.8 million from the Tourism Program. Eight of these projects were managed by third parties contracted by the Department while the Provincial marketing activities were administered by the Department of Tourism, Culture and Recreation.

Figure 2

#### Selected Projects and Agreement Funding

| Project                                                                                                                   | ERA Funding Allocated |
|---------------------------------------------------------------------------------------------------------------------------|-----------------------|
| <b>Interpretation Facilities</b>                                                                                          |                       |
| Grenfell Interpretation Centre                                                                                            | \$2.7 million         |
| Ferryland Archaeology Program                                                                                             | \$1.0 million         |
| <b>1997 Events Support</b>                                                                                                |                       |
| Replica of the Matthew                                                                                                    | \$1.0 million         |
| <b>Marketing</b>                                                                                                          |                       |
| Provincial Marketing Activities<br>(includes a third party project of \$140,000 with<br>Viking Trail Tourism Association) | \$ 2.4 million        |
| <b>Cultural Industries (Application Driven)</b>                                                                           |                       |
| Four Miscellaneous Projects                                                                                               | \$ .7 million         |
| <b>Total</b>                                                                                                              | <b>\$7.8 million</b>  |

Source: 31 March 1999 ERA Financial Summary Worksheet

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| <b>1997 Events Support</b>                                                                                                |                       |
| Replica of the Matthew                                                                                                    | \$1.0 million         |
| <b>Marketing</b>                                                                                                          |                       |
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| <b>Cultural Industries (Application Driven)</b>                                                                           |                       |
| Four Miscellaneous Projects                                                                                               | \$ .7 million         |
| <b>Total</b>                                                                                                              | <b>\$7.8 million</b>  |

Source: 31 March 1999 ERA Financial Summary Worksheet

### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

Most of the projects funded under the Agreement, including the three projects selected from Interpretation Facilities and the 1997 Events Support identified above, were specifically identified in the Agreement. Funding under the Marketing project, with the exception of the third party contract with the Viking Trail Tourism Association, is directly managed and spent by the Department for Provincial marketing initiatives. The Cultural Industries project was allocated \$2.5 million, as indicated in Figure 1, and interested organizations and individuals are required to apply for funding. Under Cultural Industries, we reviewed four projects which were approved for funding. In addition, we reviewed four applications which had been rejected to determine if, in fact, they should have been rejected.

We completed our review in February 1999. Our objectives were to:

- determine compliance with provisions of the Economic Renewal Agreement and the contracts entered into between the Province and the organization or individual receiving funding;
- determine whether approved projects were adequately monitored to ensure that projects were on schedule and that funding was spent for the purposes intended; and
- determine whether programs and various projects under each program are being adequately evaluated to ensure that the objectives of the Agreement are being achieved.

### **Conclusions**

The Management Committee has complied, for the most part, with terms of the Agreement. Our review, however, identified the following weaknesses: advance funding for one project reviewed was provided before the project was formally approved by the Committee, eligible costs were not adequately defined in all third party contracts, all calls for tenders and announcements on the award of contracts were not approved by the Management Committee, and the Management Committee did not ensure that third parties complied with all relevant Federal and Provincial legislation.

The Department is not ensuring that all third parties comply with all contract terms including the submission of a three month cash flow when requesting advances and the timely submission of internally prepared financial statements and quarterly status reports.

### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

The Department has not conducted any inspection or audit on third party records nor has it required any audited financial statements from third parties. As a result, the Department cannot demonstrate that all third party expenditures funded under the Agreement were eligible expenditures.

The Department is not adequately monitoring all projects as they near completion or as all ERA funds have been disbursed to the third party.

Although an Evaluation Framework has been established and some useful information is being provided through this Framework, adequate performance information necessary to evaluate the Tourism Program is not being provided by all of the implementing parties. In addition, since key performance targets were not included in the third party contracts there is no formal requirement for these third parties to provide this information. As a result, it will not be possible for the Management Committee to evaluate whether the objectives of the Agreement are being achieved.

#### **Findings and Recommendation**

#### **Compliance with Agreement**

Our review indicated that the Management Committee has complied, for the most part, with the Agreement. However, the following weaknesses were identified:

- A disbursement in the amount of \$150,000 relating to the Grenfell Interpretation Centre was made before the project was formally approved by the Management Committee.
- With the exception of Cultural Industry Initiatives and the Viking Trail Tourism Association, the third party contracts did not define what types of expenditures could be considered "eligible costs" and funded under the ERA program.
- Third party contracts did not contain any direction regarding the disposition of assets funded under the Agreement.
- The Agreement requires that the Management Committee approve all calls for tenders and announcements on the awarding of contracts. This responsibility was delegated by the Management Committee to the Implementation Committees. Our review of projects funded through organizations or individuals indicated that the Committees are not approving all calls for tenders and announcement of contract awards.

### 3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement

- The Agreement requires that all relevant and applicable Federal and Provincial legislation and policies apply to all projects. Examples of Provincial legislation and policies include the *Public Tender Act* and Government's policy on the awarding of consulting contracts. Compliance with this requirement has not been included in any contracts with organizations and individuals receiving funding under the Agreement. In addition, there are no policies to ensure compliance with this requirement.

In March 1999, a round table discussion was held on this issue with the objective of formulating a policy which would address the requirements of the Agreement.

#### Compliance with Contract Terms

The Agreement addresses the requirements of contract procedures for projects administered by organizations or individuals. The Agreement requires contracts with organizations or individuals to specifically include certain clauses. Our review of the eight third party contracts indicated the following:

- The third party contracts state that an advance payment may be made to the applicant based on a 3 month forecast of cash requirements. In three projects, (Grenfell Interpretation Centre, Ferryland Archaeology Project and Replica of the Matthew) advances were made without a 3 month forecast of cash requirements submitted from the third party. As a result, monies were advanced without the proper supporting documentation.
- The third party contracts also require that the applicant submit within 90 days of the end of each fiscal year, a copy of its internally prepared financial statements. In two projects, (Ferryland Archaeology Project and Viking Trail Tourism Association) financial statements had been submitted for only one year and in another project (Replica of the Matthew), no financial statements for any year had been submitted. As the Department has not conducted any inspection or audit on third party records as of February 1999 nor has it required any audited financial statements from third parties, the Department cannot demonstrate that all third party expenditures funded under the Agreement were eligible expenditures.



### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

- The third party contracts also require that the applicant shall submit quarterly status reports on the progress and results of the activity. In one project (Ferryland Archaeology Project), this requirement was not enforced by the Department due to the seasonality of the project. The accepted practice was for the third party to submit a report after the completion of each season detailing expenditures incurred with supporting documentation. However, these status reports were not received until 5-6 months after the season was completed. In another project (Viking Trail Tourism Association), only two quarterly status reports have been received since the initial disbursement in early 1997.

In reviewing the Cultural Industries project, we determined that eligibility criteria had been established for approving applications for funding. A review of four applications which had been rejected for funding indicated that in all cases there was adequate support for these decisions.

#### **Monitoring**

Effective monitoring of the progress of projects is essential to determine whether project objectives are being achieved, funds are being spent for their intended purpose and problems are detected early during implementation of the Agreement, thus providing a basis for refinement. Our review of this area indicated the following:

- As projects near completion, monitoring should continue until all ERA funds have been spent by the third party for the intended purpose. Even though the entire amount of the funding may be disbursed to the third party, the Department still has a responsibility to monitor the project and ensure that the third party remains accountable for the entire amount of the funding. In our review, instances of weaknesses in monitoring were identified as the project neared completion or the entire amount of the funding had been disbursed.

For the Grenfell Interpretation Centre, the last report received was in August 1998 which indicated that there was approximately \$30,000 remaining of ERA funding to be spent by the third party. As of audit date (February 1999), a final report detailing total ERA expenditures had not been received.

For the Viking Trail Tourism Association project, which was to be completed by 31 March 1999, there was no evidence in the project file to indicate that the Department had taken steps to monitor the project since the receipt of the last status report submitted in early 1998.



### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

Final disbursement was made in November 1998 to the Ferryland Archaeology Project. At that time, the Department requested supporting documentation for costs totalling \$11,260. As of audit date in February 1999, this documentation had not been received and the Department had not followed-up with the third party. In addition, included in the final project cost report prepared by the third party were administration expenses of \$30,000. The third party has not, however, provided any documentation to the Department to support this \$30,000 nor has the Department requested such supporting documentation.

For the Matthew Replica Project, our review of documentation indicated that the Department was extensively involved in monitoring the project. As part of the monitoring of this project, the minutes of third party meetings and project status reports were reviewed by the Department. Our review indicated that since September 1998, project status reports and copies of minutes were not on file. Although 100% of the ERA funding of \$1,000,000 has been advanced to this third party, the Department still has a responsibility to monitor this project to ensure that all funds are spent for the intended purpose and that the project objectives are achieved. Of the \$1,000,000 ERA funding, \$300,000 was designated for the construction of the Matthew Replica while the \$700,000 balance was designated towards the construction of a storage facility for the Matthew Replica. In June of 1999 we completed a tour of the Matthew Replica and the partially completed storage facility. Discussions with officials of the Matthew Legacy Committee indicated that it is estimated that an additional \$600,000 in funding is required to complete the storage facility.

- The total funding for the Provincial Marketing Program is \$2,400,000. Ninety - four percent of this funding is administered by the Department of Tourism, Culture and Recreation. The funding is to be used to assist the Province to initiate new advertising, travel trade promotions and a public relations program aimed at new and existing markets. Since this funding is being administered by the Department, monitoring and reporting of ERA expenditures under this program is not as extensive as required with third party implementation. Monitoring and reporting is best described as an informal process between the ERA coordinator and the Department.

### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

During our review it was noted that expenditures relating to fiscal years 1996-97 and 1997-98 were not being properly charged to the ERA account centre. As a result, at the end of each of these fiscal years, the expenditures incurred by the Department had to be reviewed to identify which expenditures related to the ERA program. Again in 1998-99, the ERA Financial Summary Report for the 9 months ended 31 December 1998 indicated that no expenditures had been incurred in the Provincial Marketing Program. However, ERA expenditures had been incurred but were not transferred to the ERA account centre until January 1999. Although the expenditures reviewed were eligible expenditures, in order to ensure that proper financial control is maintained, at the onset of each year, the Department should have identified specific marketing activities to be targeted for ERA funding. As well, as these expenditures were incurred, they should have been charged to the appropriate ERA account centre to facilitate monitoring of the Marketing Program.

#### **Evaluation**

To ensure that objectives of the Agreement and the various individual projects have been achieved, the Agreement required the development of an Evaluation Framework within six months of signing the Agreement and a comprehensive evaluation report within six months before the termination of the Agreement. The Evaluation Framework was to address such issues as the responsibilities for evaluation activity and data collection, the character and timing of data collection, and the provision of baseline studies, monitoring and program reports. During the review of selected projects, the following issues were identified:

- For each of the projects funded under the Agreement, Schedule B specifies various economic benefits and job creation potential. To measure the achievement of these economic benefits and job creation potential, targets or key results are required to be included in the Evaluation Framework. Our review indicated that many of these targets were not included in the Evaluation Framework. Without this information, it will not be possible to determine whether the economic benefits and job creation have been achieved.
- In many cases where targets or key results were included in the Evaluation Framework, baseline information and performance data was not available to determine whether the economic benefits and job creation has been achieved.

### 3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement

- Roles and responsibilities for data collection, including how often data should be collected and who should be collecting it, have not been adequately defined or communicated to the appropriate officials. For example, discussion with a Departmental official indicated that the responsibility for co-ordinating the collection of data for the Tourism Program has not been formally assigned to anyone. Furthermore, another Departmental official specified in the Evaluation Framework as responsible for the provision of data on several other projects was no longer working with the Department and no one had been reassigned this responsibility.
- Although performance data for certain projects is to be provided by a third party, this requirement is not included in the third party contracts for the projects that we reviewed. The data that is provided by third parties is not verified.

#### **Recommendation**

*The Department should consider our findings and take appropriate action as deemed necessary.*

#### **Department's Response**

##### ***Compliance with Agreement***

- *With respect to the initial payment on the Grenfell project, the Project Authorization was signed by the Implementation Committee on July 12, 1996, while the payment was not made until August 28<sup>th</sup>. Although the Management Committee did not sign until September 16, there was no indication in the files of any problems existing with the project.*

*The minutes of the first Management Committee of June 19, 1996 state, "The Implementation Committee presented all Project Approval forms for signatures once the Agreement is signed." The Federal Co-Chair stated that, "most of the Tourism projects have been developed in-depth over the past two years and, on that basis, the Management Committee should not have much of a problem with them." It should be noted that in addition to verbal approval from the MC, a letter of offer signed by the third party was in place prior to the initial payment.*

### 3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement

- *With respect to the observation that Ferryland, Grenfell and the Matthew Legacy are the third party contracts that did not define what types of expenditures could be considered "eligible costs" and funded under the ERA program, the following is noted: With regards to the Ferryland project, the funding is directed toward continuation of ongoing archaeology as funded by this Department and the Federal Government under the previous Cooperation Agreement. Section 7.1 of the Canada/Newfoundland Agreement on Economic Renewal states, "All eligible costs hereinafter referred to as 'the eligible costs' include reasonable costs approved by the Management Committee" [as per subsections (a) through (d)]. It is therefore reasonable that expenditure information supplied by Memorial University related to Archaeology are valid expenditures under this Agreement. Both the Archaeology and Interpretation components of this project were covered in a preliminary budget that resulted from consultation between the Colony of Avalon and staff of the Tourism component of the ERA. This budget was part of the project description attached to the PA and signed off by both Provincial and Federal officials.*

*The same document exists for the Grenfell project for which \$2.7 million was directed toward a new Interpretation Centre, interior and exterior exhibit work and site development. Again any reasonable costs associated with these activities can be considered in the payment approval process.*

*The 1997 Events Support Project Authorization includes a contribution of \$1.0 million toward the legacy project which included, the replica of the Matthew with associated interpretation centre and docking facilities. Contracts under this initiative were managed by an engineering consultant who acted as liaison with the Department and the Legacy committee.*

*While 'Preliminary Budget' information was attached to the Project Authorizations and resulted from consultation with the third parties involved, it is agreed that some formal recognition of this framework should form part of the third party contract similar to CIDI, Living Interpretation and Community Museum third party contracts.*

### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

- *Regarding the lack of direction for disposition of assets funded under the Agreement, our practice has always been consistent in this area on all cost shared agreements. The disposition of assets has been left to the discretion of the funded group. Perhaps a clearer policy in this area should be developed based on an assessment of the types of assets acquired under such a variety of projects.*
- *With respect to the Committees not approving all calls for tenders and announcement of contract awards, as pointed out, in some cases proper procedures have been followed, in other cases Committees have reviewed tender calls and awards after the fact. Even though attempts are made to monitor these activities, third party groups do not always comply. Given the scale and variety of activities it is sometimes difficult to monitor 3<sup>rd</sup> party groups to prevent this before it happens.*
- *With respect to the requirement that all relevant and applicable Federal and Provincial legislation and policies apply and are included in any contracts with organizations and individuals receiving funding under the Agreement, this item has been reviewed in conjunction with the Office of the Auditor General and other ERA participants, and options have been identified to deal with 3<sup>rd</sup> party compliance in the future.*

#### **Compliance with Contract Terms**

- *With respect to observations over this area, the comments are directed in whole or in part towards four of the eight third party contracts reviewed: Ferryland, Grenfell, Matthew Legacy and the Viking Trail Tourism Association. Although every attempt is made to monitor cash flow and progress reports, there are areas that need tightening. Often, quarterly reports are comprised of phone calls, faxes or site visits. Greater adherence is required regarding the quarterly report process.*
- *In the case of the Legacy Committee, the audited financial statements were not even available to them until some 6 months following year end.*
- *Funded parties are advised that records need to be retained for 36 months after completion of the project for possible audit purposes, but compliance with this issue is a human resource problem.*



### 3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement

#### *Monitoring*

*In several of the projects noted, monitoring of third party activities was carried out but the files lacked the appropriate paper trail essential to indicate that the project was in fact receiving the attention required. Steps have already been taken to ensure that contact with third party groups is indicated in the proper manner. Many of the comments in the previous section apply here as well. However, in terms of specifics:*

- *For the Viking Trail Tourism Association project (VTTA), while no status report had been received in that period there was communication between ERA management and the committee in terms of verbal updates. In the fall of 1998, at the request of the ERA manager, VTTA submitted a copy of the report generated from the VTTA Fall meeting. The file contains a note dated in December requesting the new manager follow up on two issues relating to this report and the balance of funding. The VTTA were subsequently contacted and a request for clarification of support for the balance of funding was made, before any consideration of issuing the final payment. Follow up early in the new calendar year indicated that the revised numbers would not be available. ERA management made arrangements to cash flow the final \$40,000 into the next fiscal year to accommodate the wishes of the VTTA committee. The VTTA produced this information in June of 1999, and final payment followed examination of the financial information.*
- *The Colony of Avalon submitted a request for final payment (\$123,060) with backup from Memorial University amounting to approximately \$111,800. The balance to be accounted for was \$11,260 and was to be supported by the Colony of Avalon with in-kind and administrative costs as per prior arrangement with ERA staff. With a group handling several million dollars during their fiscal year, finding support for the \$11,260 was only a formality and there were no concerns in terms of issuing the final payment. The committee member responsible for producing support for this balance was contacted in November. Before following through on the request this individual left work and remained off work on extended sick leave. The detail in supplying this information was not followed up on by the replacement and was not considered to be a major issue by ERA staff in terms of completing the file. The committee was again contacted early in the next fiscal year at which time support for the \$11,260 was provided as well as a copy of the year end financial statements.*



### **3.38 A Review of the Tourism Component of the Canada-Newfoundland Economic Renewal Agreement**

*The \$30,000 in administration costs cover the 96-97 and 97-98 fiscal years for which advances were made. Based on our own review of the files we would have to concur with the observation that documentation for these was not provided.*

- *With respect to the Provincial Marketing Program, the timing of the transfers is certainly an issue here and was related to staff turnover and work volume. Ideally these transfers should have been made at least on a quarterly basis. The report suggests the costs should have been charged directly to the ERA accounts however we do not agree with this analysis. There is a high volume of activity in this Division and the process of paying, tracking and transferring costs could mean redirecting of invoices to a number of appropriate account centres. Rather than have invoices charged to ERA accounts and then have to be monitored for accuracy it was better to pay the costs in the division as they occurred and journal voucher the ERA costs separately.*

#### ***Evaluation***

*Evaluation is an area that needs greater attention. The evaluation framework was the product of input from all participating departments. The problem was in establishing baseline information and as the information was not readily available within this Department but rather in the private sector, gathering any meaningful information continues to be a challenge.*

### **3.39 Labrador Ferry Service Equipment Repair**

#### **Introduction**

In March 1997 the Province signed an agreement with the Federal government to transfer responsibility for the operation of the coastal Labrador ferry service from Marine Atlantic to the Province. In exchange for assuming responsibility for the ferry service the Province received \$349.2 million in December 1997, consisting of \$340 million plus accrued interest. As part of the agreement, the Province also received the two ferry vessels used in the operation of the marine freight and passenger services (the MV Northern Ranger and the MV Sir Robert Bond), several parcels of land together with wharves and related facilities, and other equipment related to the operation of the ferry service including forklifts, fifth wheel trailers and diesel refrigeration units. The main terminal for servicing the equipment used for the coastal Labrador ferry service is Lewisporte.

In order to prepare for the 1998 ferry service season, the Province determined that repairs were required to the equipment it had received from Marine Atlantic. In February 1998, two tenders for the repair of the equipment were issued. The first tender was for the repair of forklifts, fifth wheel trailers, container handlers, a garbage truck, a back hoe, a van and an air compressor. The second tender was for the repair of 52 diesel refrigeration units. Both tenders, with the exception of some minor repairs to the van, were awarded to the same contractor. Total payments to the contractor relating to the two tenders were \$250,000 and \$77,000 respectively.

A further related contract was issued for the provision of various services relating to the former Marine Atlantic premises in Lewisporte. Total payments to the contractor relating to this contract were \$226,000.

#### **Scope and Objectives**

We reviewed a sample of expenditures incurred for repairs of equipment at the Lewisporte ferry terminal by the Department of Works, Service and Transportation from 1 April 1997 to 31 March 1999. Our objective was to determine whether the tenders were called and awarded in accordance with the *Public Tender Act*, and whether the work performed and the associated expenditures were adequately monitored.

#### **Conclusions**

##### **Tenders**

The Department of Works, Services and Transportation did not comply with the *Public Tender Act* and Government policies relating to the repair of equipment at the Lewisporte ferry terminal. For example:

### 3.39 Labrador Ferry Service Equipment Repair

- (i) The successful tender for repair of the forklifts, fifth wheel trailers, and other ferry terminal equipment was \$11,134. The final cost to complete the work specified in the tender, plus additional work completed by the contractor on the same equipment, totalled approximately \$250,000. Change orders relating to this tender were not issued in accordance with the *Public Tender Act*.
- (ii) The successful bid for the tendered repair of refrigeration units was \$34.75 per hour. However, most of the work was completed at a rate of \$42 per hour with some at \$52 per hour. The final cost to complete the work specified in the tender totalled approximately \$77,000. The Department had no authority to increase a tendered rate of \$34.75 per hour to \$42 and \$52 per hour.
- (iii) The Department of Works, Services and Transportation contravened the *Public Tender Act* when it did not call public tenders for various other services relating to the former Marine Atlantic premises in Lewisporte. These services cost \$226,000 over a six month period.

The Department of Works, Services and Transportation has weaknesses in its internal control procedures relating to purchasing and payments. Several weaknesses were evident in relation to the Department's payment of invoices including duplicate payment of invoices and payment for goods and services which were not in accordance with the contracts.

### Findings and Recommendations

#### 1. Repair of Forklifts, Fifth Wheel Trailers and Other Equipment

In February 1998, the Department called tenders for repairs to 38 forklifts, 13 fifth wheel trailers, 4 container handlers, a garbage truck, a back hoe, a van and an air compressor. The tender documents requested that bids be submitted for the completion of the work itemized on the listing which was included in the tender and that an hourly rate be provided for any additional repairs which may be required. Our review of the awarding of the tender and expenditures relating to the tender indicated the following:

##### (a) Original Cost Estimate

In accordance with Government policy a Requisition for Supplies and Services was forwarded to the Government Purchasing Agency to commence the tendering process. This requisition was required to provide information to the Government Purchasing Agency as to the nature of the work to be tendered and the estimated cost. However, the Requisition for Supplies and Services relating to this tender included an estimated cost of only \$1. As a result, it was difficult for the Government Purchasing

### 3.39 Labrador Ferry Service Equipment Repair

Agency to determine the reasonableness of the bids subsequently received and to determine whether there were sufficient funds available at the Department.

#### (b) Tender Documentation

Each contractor submitting a bid on the tendered work was required to indicate the cost required to complete repairs for each piece of equipment listed on a 12 page schedule attached to the tender document. In addition to being provided with the 12 page detailed listing of each piece of equipment and the related repairs required, the bidders also attended a public viewing of the equipment where representatives of the Department were available to explain the work required.

The tender documents required that bids be submitted in two areas as follows:

- (i) the costs to complete specific repairs to each piece of equipment indicated on the 12 page listing; and
- (ii) the hourly rate to be charged for any additional repairs identified during the initial repairs.

In the tender documents, the Department indicated the tender would be awarded based on the tendered cost of the initial repairs, and would not be based on the per hour rate quoted for any additional work.

A review of tender documents submitted by the successful contractor indicated that the 12 page schedule was not completed in detail as required by the tender. Instead, the contractor provided a global cost for repairing each class of equipment. However, the Department did not disqualify the bid submitted by the contractor for failure to comply with the requirements of the tender.



Forklifts at the Lewisporte Ferry Terminal

### 3.39 Labrador Ferry Service Equipment Repair

**Figure 1**

#### Repairs to Equipment Tender Bids Received

| Type of Equipment    | Bidder 1         | Bidder 2        | Bidder 3        | Bidder 4        | Bidder 5        |
|----------------------|------------------|-----------------|-----------------|-----------------|-----------------|
| Forklifts            | \$50,000         | \$17,871        | \$21,900        | \$24,775        | <b>\$6,995</b>  |
| Fifth Wheel Trailers | 40,000           | 9,852           | 5,557           | 11,080          | <b>3,250</b>    |
| Container Handlers   | 6,000            | 3,381           | 1,800           | 3,170           | <b>672</b>      |
| Garbage Truck (Note) | 2,500            | 1,398           | <b>140</b>      | 1,690           | No bid          |
| Back Hoe (Note)      | 600              | 208             | <b>165</b>      | 500             | 175             |
| Van (Note)           | 800              | 1,048           | <b>115</b>      | 1,490           | No Bid          |
| Air Compressor       | 300              | 239             | 50              | 300             | <b>42</b>       |
| <b>Total</b>         | <b>\$100,200</b> | <b>\$33,997</b> | <b>\$29,727</b> | <b>\$43,005</b> | <b>\$11,134</b> |

Source: Tender Summary prepared by the Government Purchasing Agency.

Note: Due to the lowest bidder declining the work for the Back Hoe, Garbage Truck, and Van, bidder number 5 was awarded the contract on the Back Hoe and Garbage Truck, and bidder number 1 was awarded the contract on the Van.

The bids received are outlined in Figure 1. The lowest bid for each class of equipment has been shaded.

#### (c) Time Frame for Completion of Tendered Work

Interviews conducted with government officials indicated that the contracted work was conducted over a period of approximately 11 weeks by 2 to 5 people. For most of the time it was reported that only 2 or 3 people were working on the tendered equipment with approximately 5 people working on the tender for the last week. During this period the Department received invoices from the contractor for approximately 3,200 hours in labor charges related to work completed at the Lewisporte terminal comprised of: 2,500 hours relating to the tender for repair of forklifts, fifth wheel trailers and other equipment, and 700 hours relating to another tender for the repair of 52 diesel refrigeration units.

No time logs or other records were maintained by the Department to substantiate the hours actually invoiced.

In the case of the repairs under the first tender, the 2,500 hours invoiced would equate to approximately 43 hours on average for repairs to each of the 58 pieces of equipment identified on the 12 page listing. Our review of invoices for which specific pieces of equipment could be determined, indicated that work completed





### 3.39 Labrador Ferry Service Equipment Repair

Figure 1

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| Type of Equipment    | Bidder 1         | Bidder 2        | Bidder 3        | Bidder 4        | Bidder 5        |
|----------------------|------------------|-----------------|-----------------|-----------------|-----------------|
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| Fifth Wheel Trailers | 40,000           | 9,852           | 5,557           | 11,080          | 3,250           |
| Container Handlers   | 6,000            | 3,381           | 1,800           | 3,170           | 672             |
| Garbage Truck (Note) | 2,500            | 1,398           | 140             | 1,690           | No bid          |
| Back Hoe (Note)      | 600              | 208             | 165             | 500             | 175             |
| Van (Note)           | 800              | 1,048           | 115             | 1,490           | No Bid          |
| Air Compressor       | 300              | 239             | 50              | 300             | 42              |
| <b>Total</b>         | <b>\$100,200</b> | <b>\$33,997</b> | <b>\$29,727</b> | <b>\$43,005</b> | <b>\$11,134</b> |

Source: Tender Summary prepared by the Government Purchasing Agency.

Note: Due to the lowest bidder declining the work for the Back Hoe, Garbage Truck, and Van, bidder number 5 was awarded the contract on the Back Hoe and Garbage Truck, and bidder number 1 was awarded the contract on the Van.

The bids received are outlined in Figure 1. The lowest bid for each class of equipment has been shaded.

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Interviews conducted with government officials indicated that the contracted work was conducted over a period of approximately 11 weeks by 2 to 5 people. For most of the time it was reported that only 2 or 3 people were working on the tendered equipment with approximately 5 people working on the tender for the last week. During this period the Department received invoices from the contractor for approximately 3,200 hours in labor charges related to work completed at the Lewisporte terminal comprised of: 2,500 hours relating to the tender for repair of forklifts, fifth wheel trailers and other equipment, and 700 hours relating to another tender for the repair of 52 diesel refrigeration units.

No time logs or other records were maintained by the Department to substantiate the hours actually invoiced.

In the case of the repairs under the first tender, the 2,500 hours invoiced would equate to approximately 43 hours on average for repairs to each of the 58 pieces of equipment identified on the 12 page listing. Our review of invoices for which specific pieces of equipment could be determined, indicated that work completed

### **3.39 Labrador Ferry Service Equipment Repair**

ranged up to 148 hours for repairs to a fifth wheel trailer and 98 hours for repairs to a container handler.

#### **(d) Work Completed**

The tender indicates what repairs are required for each piece of equipment and that the successful bidder was to be determined based on total cost (labour and materials included). The contractor invoiced the Department for the exact amount bid for each class of equipment. However, these invoices only included labour and fire extinguisher installation. The parts which would have been expected to complete the required repairs were not included. All parts were invoiced as part of the additional work required and not as part of the original \$11,134 tendered repairs. As a result, the Department paid additional monies for parts and supplies that were already included in the \$11,134 tender.

Furthermore, the tender required the contractor to obtain three quotes on any parts purchased. This was not done.

#### **(e) Duplicate Payments**

A review of the invoices relating to this tender disclosed that the Department paid two invoices twice. The total invoiced amounts were \$6,069. The invoices in question were not marked as being duplicates either by the contractor or the Department.

As evidenced by these duplicate payments, the Department did not adequately review individual invoices and overall totals for parts and labour to ensure that the amounts billed were reasonable and that goods and services invoiced were in accordance with the tendered contract. This is a significant issue since the procedures followed for payments under this contract are the same as those for all payments made by the Department.

#### **(f) Expenditures under Tendered Contract**

Batteries for lifeboats on the ferries, not included in the tender, were improperly invoiced and were paid by the Department. These amounts are not material.

#### **(g) Change Orders**

A review of expenditures under the tendered contract disclosed that three change orders were issued to the original contract of \$11,134. The original contract amount and the three change orders are detailed in Figure 2.

### 3.39 Labrador Ferry Service Equipment Repair

Figure 2

#### Repair of Forklifts, Fifth Wheel Trailers and Other Equipment Change Orders Approved

| Item              | Date Approved     | Amount           | Department's Explanation                                             |
|-------------------|-------------------|------------------|----------------------------------------------------------------------|
| Original Contract | 3 April 1998      | \$11,134         |                                                                      |
| Change Order      | 10 July 1998      | 60,610           | Extra costs incurred during repairs.                                 |
| Change Order      | 16 July 1998      | 159,000          | Extra costs incurred during repairs.                                 |
| Change Order      | 11 September 1998 | 18,275           | Extra costs on invoice numbers 43921, 43901, 43151, 42956 and 42960. |
|                   | <b>Total</b>      | <b>\$249,019</b> |                                                                      |

Source: Review of Original Contract and Change Orders

The *Public Tender Act* states change orders are to be issued "...subject to the prior approval of the head of the government funded body." Failure to obtain approval in advance is in contravention of the *Public Tender Act*. In the case of the three change orders included in Figure 2, approval came after the work authorized by the change order had been completed. For example, in the case of the third change order, approval was provided in September 1998 relating to invoices dated between 25 May to 29 July 1998.

The *Public Tender Act* also requires that, where change orders are issued and exceed certain thresholds, the Department is required to report the change orders to Treasury Board. The change orders made to this contract exceeded the thresholds indicated in the Act and as a result, should have been reported to Treasury Board. The Department did not report the change orders as required.

### **3.39 Labrador Ferry Service Equipment Repair**

#### **2. Repair of Refrigeration Units**

In February 1998, the Department called a tender for the repair of 52 diesel refrigeration units. The tender documents requested that bids be submitted for the completion of these repairs on a price per hour basis. The tender was awarded to the lowest bidder at a rate of \$34.75 per hour. This lowest bidder was the same contractor which had been awarded the contract for repairs to the forklifts, fifth wheel trailers and other equipment. The final cost to complete the work relating to this contract was approximately \$77,000. Our review of expenditures related to this tender indicated the following:

##### **(a) Original Cost Estimate**

In accordance with Government policy a Requisition for Supplies and Services is forwarded to the Government Purchasing Agency to commence the tendering process. This requisition is required to provide information to the Government Purchasing Agency as to the nature of the work to be tendered and the estimated cost. However, the Requisition for Supplies and Services relating to this tender included an estimated cost of only \$1. As a result, it was difficult for the Government Purchasing Agency to determine the reasonableness of the bids subsequently received and to determine whether there were sufficient funds available at the Department.

##### **(b) Change in Tendered Price per Hour**

On 16 March 1998, the lowest bidder tendered an hourly rate of \$34.75 for the testing and repair of refrigeration units. Documentation at the Department indicated that the hourly rate of \$34.75 was subsequently changed to \$42 per hour. The change order was issued on 10 July 1998 and the majority of invoices were paid at the increased rate of \$42 per hour. In addition, there were a number of invoices paid at the rate of \$52 per hour.

The Department could not provide any reasonable explanation for increasing the tender rate of \$34.75 per hour to \$42 and \$52 per hour. This is significant since there were two other qualifying bids less than the \$42 per hour.

There is no authority for the Department to arbitrarily increase a tendered price.

### 3.39 Labrador Ferry Service Equipment Repair

#### (c) Duplicate Payments

A review of the invoices relating to this tender disclosed that the Department paid three invoices twice. The total invoiced amounts were \$8,212. The invoices in question were not marked as being duplicates either by the contractor or the Department. In all three cases, support for the duplicate payment were photocopies of the original invoice and should have been questioned by departmental officials.

As evidenced by these duplicate payments, the Department did not adequately review individual invoices and overall totals for parts and labour to ensure that the amounts billed were reasonable and that goods and services invoiced were in accordance with the tendered contract. This is a significant issue since the procedures followed for payments under this contract are the same as those for all payments made by the Department.



Refrigeration Units at the Lewisporte Ferry Terminal

#### (d) Change Orders

A review of expenditures under the tendered contract disclosed that two change orders were issued in relation to the additional repairs identified by the contractor. The original contract amount and the two change orders are detailed in Figure 3.

The *Public Tender Act* states change orders are to be issued "...subject to the prior approval of the head of the government funded body." Failure to obtain approval in advance is in contravention of the *Public Tender Act* and could result in goods and/or services being obtained which were not requested or desired. In the case of the two change orders included in Figure 3, approval came after much of the work authorized by the change

### 3.39 Labrador Ferry Service Equipment Repair

order had been completed. For example, in the case of the second change order, approval was provided in September 1998 relating to invoices for work which had been completed two months earlier.

The *Public Tender Act* also requires that, where change orders are issued and exceed certain thresholds, the Department is required to report the change orders to Treasury Board. The change orders made to this contract exceeded the thresholds indicated in the Act and as a result, should have been reported to Treasury Board. The Department did not report the change orders as required.

#### (e) Other Expenditures under Tendered Contract

A review of other expenditures indicated that items not included in the tender specifications were improperly invoiced as part of the tender. The contractor purchased eight used refrigeration units for \$1,100 per unit plus freight of \$2,976 for a total of \$11,776. The Department paid for these items as if they were goods and services to be acquired under the tender. Since these items were not included in the scope of the original tender, the Department circumvented the *Public Tender Act* which it is responsible for administering. The Department should have tendered for the purchase of the eight refrigeration units.

Figure 3

#### Repair of Diesel Refrigeration Units Change Orders

| Item              | Date Approved     | Amount          | Details                                            |
|-------------------|-------------------|-----------------|----------------------------------------------------|
| Original Contract | 2 April 1998      | \$60,000        |                                                    |
| Change Order      | 16 July 1998      | 7,100           | Extra costs incurred during repairs.               |
| Change Order      | 11 September 1998 | 10,075          | Extra costs incurred for invoices 43517 and 43539. |
|                   | <b>Total</b>      | <b>\$77,175</b> |                                                    |

Source: Review of Original Contract and Change Orders



### 3.39 Labrador Ferry Service Equipment Repair

#### 3. Retention of Private Contractor

In March 1997, the Province signed an agreement with the Federal government which included the transfer of responsibility for the former Marine Atlantic premises in Lewisporte to the Province. In December 1997, operational responsibility for the premises was assumed by the Province and the Department entered into a contract with a private contractor to provide standby/ watchkeeping, snow clearing, claims adjudication, and security services relating to the vessels, equipment and property at that site. The initial contract provided for a total payment for these services of \$30,250 per month.

In February 1998, an amendment to the original contract was authorized whereby the private contractor would also provide cleaning and painting services relating to the MV Sir Robert Bond, and supervisory and monitoring services relating to the contracting out of the freight handling equipment maintenance. The contract amendment provided for payment for these services on an hourly basis, at \$39.60 per hour.

In April 1998, a second amendment to the original contract was authorized whereby the private contractor would provide meals on board the MV Sir Robert Bond and the MV Northern Ranger to workers engaged in retrofitting these vessels. The contract amendment provided for payment at a per diem rate of \$100.

A total of approximately \$226,000 was paid to the contractor from 1 January 1998 to 19 June 1998 for work authorized under the original contract and subsequent amendments. Our review of the contract and related payments indicated the following:

- The Department did not comply with the *Public Tender Act*, which at that time, required services exceeding \$7,500 be publicly tendered. Although the Lewisporte ferry terminal was transferred to the Province upon signing the agreement with the Federal government in March 1997, Departmental officials indicated it was not determined until December 1997 when operational responsibility was finally transferred that security services had not been arranged. As a result the Department considered such services to be urgently required. However, given the length of time between when the transfer agreement was signed in March 1997 and December 1997, it would be expected that this situation should have been foreseen.
- A review of individual invoices indicated that the Department paid invoices for services covered by the first contract amendment before the contract was actually amended.

### 3.39 Labrador Ferry Service Equipment Repair

- One invoice for supervisory and monitoring services included charges for 21 hours at the rate of \$42 per hour although the rate authorized in the contract amendment was \$39.60 per hour.

#### 4. Monitoring of Equipment Repairs

The Department did not retain sufficient documentation to enable a review of the work completed on the tenders. For example, there was no documentation at the Department in the form of work orders, to support the repairs indicated as being required although the work orders served as authorization and support for work performed. Officials of the Department indicated that the work orders were retained by the company hired to monitor the work performed by the contractor undertaking the repairs.

In addition, the Department did not maintain a log of the hours spent by the contractor repairing the equipment.

A Departmental official indicated that the time proposed by the contractor for each repair would have been compared to industry standards by the company hired to oversee the work performed, to determine if the time proposed was reasonable for purposes of preparing a related work order. The Department could not locate a copy of the industry standards that the previous owners of the equipment (Marine Atlantic) had provided when the equipment was transferred to the Province.

As a result of not being able to locate the industry standards, the Department could not determine the reasonableness of the amounts it paid for each repair completed. We were informed that these standards were provided to the private contractor hired to oversee the work performed on the equipment.

#### Recommendations

*The Department should comply with the Public Tender Act and Government policies.*

*The Department should undertake a review of its internal control procedures relating to purchasing and payments.*

### **3.39 Labrador Ferry Service Equipment Repair**

#### **Department's Response**

##### **1. Repair of Refrigeration Units**

*The lowest bid price received for the start up and testing of the refrigeration units was \$34.75 per hour from [the contractor]. For that rate, the contractor was required to perform initial start up and testing of units to their full capacity (Appendix A of TP #553365). The Appendix also indicated that 'additional' work would be based on a flat rate basis. The contractor was not compelled to perform the additional work at the \$34.75/hour rate. The flat rate was arrived at through negotiation with the Department whereby an estimate of repair hours (within industry standards) was given for each piece of equipment. The number of repair hours was multiplied by the mutually agreeable \$42.00/hour rate which provided the total flat rate cost per price. The Department representatives ensured that the final invoices matched the flat rate previously agreed upon before processing for payment. I am advised that there were no instances where the Department paid a rate of \$52.00/hour for the additional work.*

*Given the Department's position of urgency of the requirement, Section 9 of the Public Tender Act could apply. The \$42.00/hour rate was considered by the Department representatives to be fair and reasonable in the context that it was the same rate for additional work as quoted in the tender for the forklifts, fifth wheel tractors, etc. The Director of Government Purchasing Agency has been consulted and agrees with the above circumstance. He has indicated that the only discrepancy in the handling of the tender for the refrigeration units was the failure to report to the House of Assembly in accordance with Section 10 of the Public Tender Act for urgent requirements.*

##### **2. Repair of Forklifts, Fifth Wheel Trailers and Other Equipment**

*In January 1998 my Department was faced with the task of assuming responsibility for and repairing a multitude of equipment in order to be ready for the May 1998 Labrador Coastal Ferry Service. If time had permitted, a detailed assessment of each piece of equipment would have been undertaken and a decision regarding repair versus retirement/replacement would have been made. Time, however, was not in our favour and to ensure that the scheduled start up of the Coastal Labrador shipping season was to be met, my Department had little choice but to do a cursory check of the equipment and perform repairs as necessary. Upon initial assessment, a listing of known repairs was compiled and submitted for public tender. From the very beginning the Department knew that, as the equipment was opened up, further repairs would be required. Therefore, bidders were instructed to price the known*

### **3.39 Labrador Ferry Service Equipment Repair**

*work and be prepared to provide fixed quotations on additional repairs at the rate quoted.*

*At the bidders conference the Department went through a 12 page work sheet in detail outlining every piece of equipment and answered any questions from bidders. The bidders were instructed to quote a labour only price for the specific work outlined. Parts and materials would be invoiced separately.*

*Since there was no way of knowing the extent of additional repairs, a number of Change Orders were issued. It is recognized by the Department that it was appropriate to issue the Change Orders before the work was carried out. However, given the pressure to meet the shipping season start up, little time was available to process Change Orders before carrying out the work. The Change Orders were subsequently issued later. General authority was given to the Executive Director of the Marine Services Branch, under Section 7 of the Public Tender Act, to do what was necessary to get the repairs done expeditiously.*

*It is emphasized that every piece of equipment was assessed for additional repairs and a firm price for repair allocated to each. The price consisted of an agreed number of repair hours (within industry standards) multiplied by the price per hour as quoted on Purchase Order 311331 (\$42.00/hour).*

*In conclusion, I do agree that Change Orders were not issued in accordance with the Public Tender Act, primarily due to the nature and time frame of the task placed on my Department. Also, there is a requirement for my Department to report the Change Orders to Treasury Board. I have taken steps to remedy this situation in the future.*

#### **3. Retention of Private Contractor**

*Upon conclusion of the Agreement in 1997 to assume responsibility for the services primarily operated by Marine Atlantic, my Department was under the understanding that Marine Atlantic employees would continue to maintain the Lewisporte terminal until February 15, 1998. However, on December 23, 1997 we were advised that all involvement of Marine Atlantic would cease as of December 31, 1997. This situation placed my Department in a circumstance where immediate action was necessary to take over responsibility for the Lewisporte terminal. With only days to act, we decided to contract the services of a previous manager of the Lewisporte terminal. A 'Contract for Services' was issued (December 29, 1997) to take effect as of midnight December 31, 1997. The following services were originally provided as per the Contract:*

### 3.39 Labrador Ferry Service Equipment Repair

1. *Standby/watchkeeping services to the M/V 'Sir Robert Bond' and the M/V 'Northern Ranger' at a per month cost of \$20,000 or a pro-rata portion thereof, if services terminate in less than one month increments.*
2. *Snow clearing services to oil tanks and both vessels to assist in case of fire emergency services at a per month cost of \$2,000 or a pro-rata portion thereof, if services terminate in less than one month increments.*
3. *Adjudication of coastal freight claims at a per month cost of \$2,000 or a pro-rata portion thereof, if services terminate in less than one month increments.*
4. *The provision of security services for all properties, equipment and vessels at a per month cost of \$6,250 or a pro-rata portion thereof, if services terminate in less than one month increments.*
5. *The Contractor will maintain a daily log for each vessel to record ambient temperatures in different sections of the vessels with recordings to be logged at least three times per day.*

*Subsequently, on February 6, 1998 the Contract was amended to include the following:*

6. *The Contractor will provide cleaning and painting services to the satisfaction of the Department on board the M/V 'Sir Robert Bond' in advance of the close of tender bids in relation to the operation of the aforesaid vessel on the Labrador Coastal Service at a per hour rate of \$39.60. These services are in addition to, and separate from, the services provided for in the original contract.*
7. *The Contractor will provide supervisory services, productivity monitoring, materials/tools control and equipment positioning in support of the contracting out of the freight handling equipment maintenance at Lewisporte at a per hour rate of \$39.60. These services are in addition to, and separate from, the services provided for in the original contract.*

*A final amendment to the Contract on April 14, 1998 added the following:*

8. *The contractor will provide meals on board the M/V 'Sir Robert Bond' and the M/V 'Northern Ranger' to workers engaged in retrofitting these vessels in preparation for the operation of the aforesaid vessels on the Labrador Coastal Service at a per diem rate of \$100.00. These services will include the provision and preparation of meals, including the purchase of all foodstuffs and the serving of*



### **3.39 Labrador Ferry Service Equipment Repair**

*the meals and are in addition to, and separate from, the services provided for in the original contract.*

*Once the contractor was onsite at Lewisporte on a full time basis, it was impractical to call for tenders for items related to the servicing and upkeep of the vessels and terminal. The contractor was totally familiar with the operation. Some of the services identified were on an 'as required' basis, i.e. snow clearing and equipment positioning for equipment repairs. Other services required the background experience of the contractor, i.e. adjudication of freight claims, provision of meals on board the M/V 'Sir Robert Bond' and M/V 'Northern Ranger'.*

*In the case of painting of the M/V 'Sir Robert Bond', I understand that three prices were received from the local area with [the private contractor] being the lowest rate.*

*In general, it did not make reasonable sense to contract related services where a contractor was already in place to oversee the operation at Lewisporte. While some of the services under the contract could have been unbundled from the technical services provided, in accordance with Section 2(g) of the Public Tender Act, it was not unreasonable given the circumstances to proceed as we did. However, I do agree that the issue should have been discussed with and approved by Treasury Board.*

*Your letter also refers to "weaknesses in its internal control procedures relating to purchasing and payments. Several weaknesses were evident in relation to the Department's payment of invoices including duplicate payment of invoices and payment for goods and services which were not in accordance with the contracts."*

*In regard to these weaknesses in internal control procedures, I have initiated discussion with our Accounting Division and instructed that steps be implemented to remedy the situation.*

#### **4. Monitoring of Equipment Repairs**

*A final point I wish to raise refers to 'Monitoring of the Equipment Repairs.' I do not feel that your comments are a true reflection of the situation. Upon reviewing with our Regional staff, I understand that the following actions took place with respect to monitoring the repair work at Lewisporte:*

- *Department oversaw the initial test to decide on tender requirements for each piece of equipment.*



### 3.39 Labrador Ferry Service Equipment Repair

- *Department hired a clerical person to provide historical data on the equipment.*
- *Through [the private contractor], the Department placed a person to 'coordinate' work orders for each piece of equipment.*
- *Each piece of equipment had a separate file outlining all necessary additional repairs.*
- *The coordinator compared times for each job with industry standards. This was reviewed by Department officials and found to be satisfactory.*
- *Each invoice was compared to the work order and signed for payment.*
- *The Department had two people continually at Lewisporte to monitor, inspect and report.*
- *Two Regional management staff visited Lewisporte weekly for monitoring, status and signing off invoices for work completed.*
- *A log was kept by the Department for each piece of equipment.*

*I do acknowledge that we did not keep a record of time for the contractor's personnel, however, this was not deemed to be necessary since each piece of equipment had a flat rate repair amount. My staff were only interested in seeing that the equipment was repaired before our deadline and for the agreed up front cost.*

*I thank you for the opportunity to respond to your letter and for our meeting of January 6, 2000. As I indicated to you, the application of the Public Tender Act in relation to Marine Services is very difficult given the nature of emergency operations and unknowns. I will be seeking an amendment to the Public Tender Act this Spring to reflect these difficulties. Also as agreed, I will make best efforts to deal with the pre-approval process of Change Orders under Section 5 or formalize the application of Section 7. With respect to regulatory requirements under the Public Tender Act, Section 5, please be assured these will be done.*

### **3.39 Labrador Ferry Service Equipment Repair**

CHAPTER

4

UPDATE ON PRIOR  
YEARS' REPORT ITEMS



## CHAPTER

## 4

Update on Prior Years'  
Report Items

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| General and Environmental Management Practices             | 1994        | 4.11        | 503 |
| <b>Department of Works, Services and Transportation</b>    |             |             |     |
| Vehicle Fleet Management                                   | 1997        | 3.12        | 506 |
| Government Purchasing Agency - <i>Public Tender Act</i>    |             |             |     |
| Exception Policy                                           | 1997        | 3.13        | 511 |
| <b>Department of Industry, Trade and Technology</b>        |             |             |     |
| The Economic Diversification and Growth Enterprises Act    | 1996        | 3.3         | 513 |
| The Privatization of Newfoundland Hardwoods Limited        | 1997        | 3.16        | 515 |
| <b>Department of Health and Community Services</b>         |             |             |     |
| Faculty of Medicine of Memorial University of Newfoundland | 1997        | 3.19        | 515 |

## **Update on Prior Years' Report Items**

### **4.1 Introduction**

We conduct legislative audits to provide the House of Assembly with information on public sector accountability. Legislative audits are carried out to determine whether:

- public money is being properly collected and accounted for;
- expenditures are properly recorded and made for the purpose intended;
- accounts are properly kept;
- assets are adequately safeguarded; and
- accounting and management systems and practices are adequate.

These legislative audits also determine whether the activities of Government departments and agencies have been carried out in compliance with legislation, government policies and other authorities.

Monitoring the implementation of our recommendations is an important part of our obligation to report to the House of Assembly. Our objective is to monitor and report the degree to which positive change has occurred as a result of the implementation of recommendations in our prior years' reports.

In 1996, we commenced a formal process of monitoring and updating the comments and recommendations included in our previous Annual Report to the House of Assembly. It is our intention to monitor and update the recommendations in each Annual Report two years after it has been issued. Monitoring will continue until we are reasonably satisfied that issues are being adequately addressed or are no longer valid.

This chapter includes the results of these monitoring activities on our 1994, 1995, 1996 and 1997 Annual Reports.

## **Department of Finance**

### **4.2.1 Newfoundland Municipal Financing Corporation (1995 Annual Report, Part 3.13)**

#### **Introduction**

The Newfoundland Municipal Financing Corporation is a Crown agency established under the authority of the *Municipal Financing Corporation Act*. The Corporation provides long-term financing for the capital requirements of municipalities. The Corporation raises funds to refinance municipal loans by the issuance of debentures in the bond market. In 1995, we concluded that there was inadequate information on the financial



## Update on Prior Years' Report Items

position of the Corporation and how the municipal debt affects the Province's financial position, assumptions used in cash flow forecasting were inaccurate and action to reduce loan arrears was not successful

In 1997 and 1998, we updated our comments of the Corporation's action in response to our 1995 comments and recommendations. We reported that the cash position of the Corporation had improved due to municipalities refinancing loans with the banks and the Province advanced \$12 million to mitigate arrears with respect to municipal loans. However, the Corporation had still not addressed the problem of delinquent accounts, the validity of certain cash flow assumptions was questionable and the Corporation's loan system still did not provide information on loan amounts paid by the Province and municipalities.

### Update

Although the Corporation has addressed some of the findings and recommendations made in our 1995 Annual Report, all issues have not been resolved as outlined below.

### Financial Position

Although its cash position has improved since our 1995 review, the Corporation has still not addressed the problem of delinquent accounts. Since 1995 the Province has provided the Corporation with a \$17 million reserve fund to lessen the impact of the arrears and reduce the number and value of delinquent accounts. However, as Figure 1 shows, the delinquent accounts identified as loan installments due and unpaid continue to increase even though \$12.2 million of the reserve fund has been allocated to 18 municipalities to assist them in meeting their debt obligations.

Figure 1

### Newfoundland Municipal Financing Corporation Financial Position 31 March (\$ 000's)

|                                 | 1999              | 1998              | 1997              |
|---------------------------------|-------------------|-------------------|-------------------|
| <b>Assets</b>                   |                   |                   |                   |
| Cash                            | \$ 10,171         | \$ 15,798         | \$ 63,768         |
| Loan instalments due and unpaid | 14,235            | 9,194             | 5,492             |
| Accrued interest receivable     | 10,063            | 11,255            | 12,287            |
| Other investments               | 29,147            | 10,957            | -                 |
| Loans receivable                | 336,128           | 343,941           | 386,655           |
| Deferred charges                | 1,485             | 1,607             | 2,121             |
|                                 | <b>\$ 401,229</b> | <b>\$ 392,752</b> | <b>\$ 470,323</b> |
| <b>Liabilities and Deficit</b>  |                   |                   |                   |
| Accounts payable                | \$ 43             | \$ 84             | \$ 48             |
| Accrued interest                | 12,896            | 13,907            | 16,023            |
| Debenture debt                  | 372,802           | 365,239           | 442,541           |
| Deferred revenue                | 8,675             | 6,041             | 4,511             |
| Reserve fund                    | 10,938            | 11,304            | 9,000             |
| Deficit                         | (4,125)           | (3,873)           | (1,800)           |
|                                 | <b>\$ 401,229</b> | <b>\$ 392,752</b> | <b>\$ 470,323</b> |

Source: Audited Financial Statements



## Update on Prior Years' Report Items

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| Accrued interest                       | 12,896            | 13,907            | 16,023            |
| Debenture debt                         | 372,802           | 365,239           | 442,541           |
| Deferred revenue                       | 8,675             | 6,041             | 4,511             |
| Reserve fund                           | 10,938            | 11,304            | 9,000             |
| Deficit                                | (4,125)           | (3,823)           | (1,800)           |
|                                        | <b>\$ 401,229</b> | <b>\$ 392,752</b> | <b>\$ 470,323</b> |

Source: Audited Financial Statements

## **Update on Prior Years' Report Items**

### **Cash Flow Forecasts**

The Corporation's most recent cash flow forecast was prepared in July 1999. This forecast projected a cash deficit of \$35.0 million, assuming no additional borrowing and lending, by the year 2014 when all current loans receivable are collected and all debentures are repaid. This is a small improvement over the 1995 forecast which projected a cash deficit of \$39.0 million by 2013 under the same assumptions.

### **Impact of Municipal Debt**

The Corporation's accounting system still does not provide information on loan amounts paid by the Province and municipalities. According to the Corporation's 1998-99 financial statements it received \$83.0 million in principal and interest payments related to regular municipal debt repayments and \$17.4 million from the chartered banks as a result of refinancing. Information received from the Department of Municipal and Provincial Affairs disclosed that in 1998-99 the Province paid \$63.8 million (77%) of the \$83.0 million while municipalities contributed \$19.2 million (23%) including \$5.4 million allocated from the reserve fund. The Province's portion has increased over the 1995 report when it contributed 65% of the total. This increase can partly be explained by the refinancing of the municipal portion of loans with the chartered banks.

The Corporation's new loan system started running parallel to the old system in September 1998. This new system will provide information on loan amounts paid by the Province and municipalities. However, as of 31 October 1999 the new system was still running parallel and many of the reports, including a report to provide the loan amounts information, were still under development.

## **4.2.2 Current Account Revenues (1995 Annual Report, Part 3.14)**

### **Introduction**

In 1994, we conducted a review of the audit and collection activities for retail sales tax at the Department of Finance. In 1995, we extended our review of retail sales tax collection activities and also conducted an additional review of the audit and collection activities for gasoline, tobacco and payroll taxes.

In 1995, we concluded the following with respect to the Department's audit and investigation systems and practices:

- efforts to identify unregistered businesses for retail sales tax and payroll tax were inadequate;

## Update on Prior Years' Report Items

- there was no regular review or monitoring of taxpayer's information returns for gasoline, tobacco or payroll taxes to ensure they were complete, accurate and filed by the required deadlines;
- management information systems were inadequate, resulting in a lack of readily available information on which to base the selection of registrants for audit, or to identify those taxpayers who were not complying with tax legislation;
- there was no systematic process for the selection of tax audits for gasoline, tobacco or payroll taxes;
- audit coverage for gasoline, tobacco and payroll taxes was low which impeded the enforcement of tax legislation; and
- once audits were selected, they were not adequately planned nor conducted in a consistent manner.

With respect to the Department's tax collection systems and practices, we concluded that:

- collection policies for retail sales tax and payroll tax needed to be clarified and more rigorously enforced;
- the Department did not always comply with collection policies relating to the suspension and termination of licences and the placing of delinquent taxpayers on Government's payment interception list;
- there was inadequate supervision of collection activities for retail sales tax and payroll tax;
- the Department had not established any program objectives or performance indicators, and there was no operational planning performed to ensure that adequate tax enforcement and collection activities were planned; and
- the Department was not providing the House of Assembly with information that is required to hold the Department accountable for its use of public resources in conducting tax audit and collection activities.

During 1997 and 1998, we asked the Department of Finance to inform us as to the progress made on our 1995 recommendations. We noted that the Department had taken action on some of our recommendations; however, many still needed to be addressed.

## **Update on Prior Years' Report Items**

### **Update**

During October 1999, in response to our request, the Department of Finance informed us as to any further progress on our 1995 recommendations.

In relation to our recommendations in the area of audit and investigation systems and practices, the Department indicated it was currently in the process of designing and implementing a new computerized tax management information system. As well, it described other recent initiatives which will increase audit coverage, including a cooperation agreement with the Federal Government covering tax evasion, tax avoidance and the underground economy.

In relation to our recommendations in the area of tax collection systems and practices, the Department indicated that with the implementation of the Harmonized Sales Tax, the value of arrears will be reduced and that it was presently reviewing its doubtful accounts for recommendation to Treasury Board for write-off. As well, it was indicated that the new computerized tax management information system currently being designed and implemented, will provide the necessary information to monitor the collection process. Furthermore, the Department will consider the preparation of an annual report in conjunction with a Strategic and Operational Plan for the 1999-2000 fiscal year.

### **4.2.3 Review of Government's Pension Plans (1997 Annual Report, Part 3.10)**

#### **Introduction**

In our 1997 Annual Report to the House of Assembly, we reported on our review of the pensions paid by the Province of Newfoundland Pooled Pension Plan from 1 January 1987 to 31 December 1996. The objectives of this review were to assess the adequacy of management systems and practices for determining eligibility for pension benefits and for monitoring continuing eligibility of beneficiaries, and the adequacy of financial and other information for reporting on the pensions managed by the fund.

Our review found that two of Government's pension plans already require deficiency payments while the two larger pension plans will require deficiency payments in 2004 and 2019, pensioners were being hired for positions in Government although Government policy forbids this unless approved by Cabinet, and there was no follow up on disability pensions to determine whether recipients could return to work.



## Update on Prior Years' Report Items

### Update

In response to our findings the Department has indicated that the monitoring of pension plans is ongoing and modifications have been made to the Public Service Pension Plan and the Teachers Pension Plan, including special payments, to address the unfunded liabilities. In 1997 and 1998, Government made two special payments of \$30 million each to the Public Service Pension Plan and will continue to make, in accordance with legislation, special payments of at least \$40 million per year until the pre-1980 debt is retired. In 1998, Government made a special payment of \$166 million to the Teachers' Pension Plan. Government will again make a special payment of \$166 million in 1999 and will continue to pay \$76 million per year until the pre-1980 debt is repaid.

The Uniformed Services Pension Plan and the Members of the House of Assembly Pension Plan continue to rely on deficiency payments from the Province to assist in meeting the pension obligations. In 1999 the MHA Plan was modified to reduce benefits and increase contributions from 8% to 9% of pensionable salary as a first step in addressing the unfunded liabilities.

Government has adopted a hiring policy with regard to the employment of pensioners which directs that pensioners are not to be hired unless there is no other candidate with the appropriate qualifications for the position, and such appointments have been approved by Cabinet.

The Department is currently assessing the need to establish a tribunal to hear appeals of disability pension applications but, as yet, Government has not been asked to consider a definite proposal.

## Department of Justice

### 4.2.4 Registrar of the Supreme Court (1994 Annual Report, Part 4.7)

#### Introduction

The Estates Office of the Registrar of the Supreme Court of Newfoundland administers the estates of deceased persons upon appointment by the Supreme Court and the trusts of minors and mentally disabled persons upon appointment by the Court or by virtue of the *Mentally Disabled Persons' Estates Act*. It also administers funds paid into Court or to the Registrar under various statutes, including the *Judicature Act*. The financial statements of the Registrar for the year ended 31 March 1999 reported total assets held in trust of \$20 million.

## **Update on Prior Years' Report Items**

### **Update**

In 1994, we concluded that practices followed by the Registrar in fulfilling legislated responsibilities were inadequate. We made recommendations at that time to assist the Registrar in the stewardship role of acting in the best interest of clients.

As we reported in 1998, the Registrar has taken satisfactory action on most of our recommendations made in 1994. However, with respect to the other recommendations for the improvement of stewardship at the Estates Office, the status of the action taken is outlined as follows:

#### **Closing of Estate Files**

##### **1994 Recommendation**

*A systematic basis for anticipating the expected date of closure of files (deceased persons) and final discharge of estates should be implemented to ensure accounts do not remain outstanding for unreasonable lengths of time in future.*

##### **Action Taken**

The Registrar indicated that, as previously reported, no formal basis has been developed to anticipate the date of file closure for deceased persons' estates. Although most deceased persons' estates have the same routine tasks that need to be done (i.e. statutory notices, taxes, clearances, etc.), there are many estates that have other issues that require them to remain active for an indeterminable period. Thus, the date of file closure cannot be anticipated. The Registrar indicated that, as previously noted, all current or on-going files are regularly reviewed and the number of older files continues to be reduced.

#### **Delays in Handling Client Matters**

##### **1994 Recommendation**

*Administrative matters such as filing required documents on behalf of clients, should be dealt with on a timely basis and policies should be developed to document the process of handling these various matters. These policies should include a requirement that all files be reviewed on a regular basis to identify outstanding matters.*

##### **Action Taken**

The Registrar indicated that, as previously reported, the Estates / Trust policies and procedures section of the manual remains incomplete. Although most policies are now in place, not all have been formalized in the manual.

## **Update on Prior Years' Report Items**

### **Policies and Procedures Manual**

#### **1994 Recommendation**

*Standard policies and procedures relating to the administration of estates and trusts should be implemented to ensure all necessary actions are performed on a regular basis. These should be formally documented by way of a manual issued to all staff.*

#### **Action Taken**

The Registrar indicated that the completion of the manual is still on-going.

### **4.2.5 Office of the High Sheriff (1994 Annual Report, Part 4.8)**

#### **Introduction**

The Office of the High Sheriff acts as the enforcement arm of the Supreme Court of Newfoundland and is responsible for jury management and court security in the Province. The Office also enforces judgements issued by the Court including the service of criminal and civil documents, executions and the seizing and selling of real and personal property.

The Office of the High Sheriff began preparing financial statements in 1992-93. Our Office has performed attest audits on these financial statements since that time. For the years ended 31 March 1993 and 1994, we issued a denial of opinion due to serious deficiencies in internal controls which made it impossible to gather sufficient, appropriate audit evidence to render an opinion. At that time, a recommendation was made to ensure the Office of the High Sheriff took immediate steps to address these deficiencies with the objective of obtaining an unqualified auditor's opinion.

In 1996, we reported that we considered the progress on the recommendations to be satisfactory in all areas. Actions taken have resulted in an unqualified opinion being expressed on the financial statements of the Office of the High Sheriff for 31 March 1996, and subsequently for 1997 and 1998. In 1996, we also reported that further required improvements in internal controls were to be addressed during the design of a new accounting system in conjunction with the passage of the *Judgement Enforcement Act*. Such improvements include the use of a computerized general ledger and the ability to produce periodic reports for monitoring of financial operations. The *Judgement Enforcement Act* and a new computerized accounting system were implemented on 1 June 1997. In addition, the enforcement of small claims judgements was added to the mandate of the Office of the High Sheriff. This has added greatly to

## **Update on Prior Years' Report Items**

the workload of the Office of the High Sheriff and resulted in additional staff being hired during 1997-98.

### **Update**

During our audit of the financial statements of the Office of the High Sheriff for the year ended 31 March 1998, we reviewed the new computerized accounting system that was implemented on 1 June 1997. Our review indicated that controls are in place to ensure the authorization, accuracy and completeness of financial transactions. We also determined that the new system provides the Office of the High Sheriff with the ability to produce periodic reports for the monitoring of financial operations.

## **Department of Education**

### **4.2.6 Memorial University of Newfoundland (1994 Annual Report, Part 4.9)**

#### **Introduction**

In 1994 and again in our updates in 1996, 1997 and 1998, we concluded that the Department of Education did not have an adequate system of accountability in place over grants paid to Memorial University of Newfoundland. In addition, although the House of Assembly approved funding to the University during 1998-99 for approximately \$120 million, there was inadequate accountability over this funding.

As a result of our review we recommended that a system of accountability be established over grants to the University. This system should include, but not be restricted to, the following components:

- Roles, responsibilities and duties of the Department of Education and Memorial University should be well defined and communicated. These should be included in legislation and further defined in policy.
- There should be adequate reporting to the Department of Education and the House of Assembly. This includes both financial and performance monitoring.
- The system of accountability should be strengthened by an independent audit process to assess the fairness of the University's representations on performance and to assess management systems and controls.

### **Update**

No action has been taken to establish an adequate system of accountability over grants paid to Memorial University of Newfoundland.

## **Update on Prior Years' Report Items**

### **Department of Environment and Labour**

#### **4.2.7 General and Environmental Management Practices (1994 Annual Report, Part 4.11)**

##### **Introduction**

In 1994 we conducted a review of the management practices and environmental management and control activities of the former Department of Environment and Lands. Our review was designed to assess whether policies and procedures were adequate to ensure compliance with relevant legislation and standards. We concluded that, in general, most aspects relating to the Department's management practices were not adequate and should be improved. In addition, the policies and procedures for environmental management and control activities were not adequate to ensure that the Department and all individuals and companies who emit pollutants into the environment (i.e. dischargers) complied with relevant legislation and standards.

In 1996, 1997 and 1998, following our review of action taken by the Department, we concluded that the recommendations in our 1994 report had not been adequately addressed.

##### **Update**

In June 1999, we contacted the Department to determine if any further action had been taken on our 1994 recommendations. The Department's response to each of these recommendations is outlined below.

##### **Management Practices**

##### **1994 Recommendations**

*The Department should establish strategic and operational plans.*

*The Department's annual report should provide sufficient information on a timely basis to assist the Legislature in holding the Department accountable for its use of public resources.*

*The Department should continue its efforts to improve the roles, responsibilities and reporting relationships within its regional offices.*

*The Department should review its human resource management policies to address such areas as performance evaluations, employee training needs, position descriptions, and the monitoring of leave entitlement.*

##### **Action Taken**

The Department indicated that it has completed an extensive planning exercise involving all staff with the aid of an external consultant. This

## **Update on Prior Years' Report Items**

process and its outcome was used to form the Department's participation in the Government-wide business planning process that commenced in the 1998-99 fiscal year. The Department reported that it has a business plan in place for the current year that contains both a strategic and an operational component.

The Department has not prepared an annual report for submission to the House of Assembly since 1991-92. The Department's intention is that its business plan and annual update will serve the same accountability function as an annual report. The business plan will set out a course of action and the update will report on progress achieved.

The Department indicated that regular meetings are being held between the Department's executive and regional staff. Regional staff have been fully involved in Departmental team building and planning initiatives. A Memorandum of Understanding has been concluded with the Government Services Centre which conducts most inspections undertaken by the Department.

The Department indicated that its Training Unit has developed a performance management system called Supervising for Success. This system is linked to their business planning process and ties key responsibility areas to lines of business. The Department's executive is committed to full implementation of this program in 1999-2000.

The Department also indicated that a comprehensive training needs assessment was completed in 1998-99. Training has been completed in most major information technology areas, negotiation skills and a number of specific scientific or technical areas. All managers are enrolled in Frontline Leadership Training, a program which will continue in 1999-2000.

The Department also reports that all position descriptions and leave entitlements are up to date.

### **Environmental Management and Control Activities**

#### **1994 Recommendations**

*The Department should review existing legislation to ensure it is current and consistent with Departmental objectives.*

*The Department should maintain a current and complete inventory of all dischargers, discharges and discharge points.*

*The Department should ensure compliance with the Waste Material Disposal Act prior to the issuance of a certificate of approval to operate a*



## **Update on Prior Years' Report Items**

*waste disposal site or waste management system. Supporting documentation should be retained and appropriately filed to indicate compliance with legislation.*

*A monitoring process to test the reliability of discharger information being submitted to the Department should be developed and implemented for water pollutants.*

*The Department should consider increasing existing inspection coverage and developing a process to obtain certification from third party inspectors regarding the adherence of applicable permit terms and conditions.*

*Controls should be strengthened to ensure that annual inspections of PCB storage sites are performed, reports are properly completed and deficiencies followed up. The files should also contain evidence of overall review and approval of the inspections by senior management.*

*The Department should determine the extent and severity of non-compliance with legislation and implement procedures to bring dischargers into acceptable compliance over a reasonable period of time.*

### **Action Taken**

The Department reported that all of its legislation is currently under review to ensure that it is relevant and appropriate. It is hoped to have all legislation reviewed and updated over the next two years.

The Department indicated that it maintains a database of effluent data from major industries plus all municipal discharge points. As well, an IT Plan is under development which will serve to refine and improve this database.

In conjunction with the Government Service Centre which enforces the *Waste Material Disposal Act*, the Department is employing its best efforts to ensure compliance with this Act.

The Department indicated that the policy on lab accreditation ensures lab analysis of samples meets all quality control standards. Industrial labs are visited, sampling procedures checked and duplicate samples taken where warranted.

The Department indicated that inspections have been and continue to be improved within available resources. The approach of using third party inspectors has been investigated and the Department has determined that it offers no major advantages over the current approach.

## **Update on Prior Years' Report Items**

The Department reported that the Government Service Centre endeavours to ensure required inspections of PCB storage sites are carried out. Inspection and inventory databases are being developed. Improved inspections and documentation is expected once these databases are completed.

The Department reported that within existing resources, it works through various means, including compliance agreements, to bring dischargers into compliance.

## **Department of Works, Services and Transportation**

### **4.2.8 Vehicle Fleet Management (1997 Annual Report, Part 3.12)**

#### **Introduction**

In 1997, we conducted a review of the Fleet Management Branch of the Department of Works, Services and Transportation to assess the adequacy of systems and processes used in the planning of the transportation needs of Government and in the acquisition, operation, maintenance, replacement and disposition of Government's light vehicles.

Minute of Council 1272-79 assigned the Department of Works, Services and Transportation with the responsibility for the efficient and effective management of Government's fleet of light vehicles including cars, station wagons, 4-wheel drives, vans and small trucks. A Fleet Management Branch was created within the Department's Maintenance Division to develop and implement policies and procedures to facilitate the management of these vehicles. The Branch is also responsible for providing support and direction to all Government departments in ensuring the effective implementation of, and compliance with, these policies and procedures. Each department has a designated Fleet Management Contact person to act as a liaison with the Fleet Management Branch. In addition, the Department operates a network of 50 vehicle repair facilities (depots) and refueling sites located throughout the Province.

Our review indicated that the Department's processes for managing Government's Vehicle Fleet were not adequate. For example:

- While the size of the fleet had been decreasing, Government could not justify its complement of light vehicles.

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- Departments did not provide adequate documentation to justify the need for the new vehicle acquired and there was no evidence that these vehicles were the most economical vehicles available to meet the transportation needs of Government. In addition, cost information to assess alternatives to purchasing vehicles was not available.
- The computerized information system used to facilitate the management of Government's light fleet produced information that was not timely, complete, accurate or understandable. As well, most users of reports produced by this system indicated that they did not review or analyze the information provided. As a result, the costs of maintaining Government's light vehicles and the extent of their usage was not being adequately monitored.
- The Department could not provide us with a listing indicating which department or which vehicles had been provided with the 1,448 computerized keys for refueling that had been issued which access the refueling site.
- For a sample of 12 vehicles which had been disposed of, 4 credit cards were identified which were still active even though the vehicles had been sold for several months. As a result of inadequacies of the Department's Computer System to capture information by transaction date, we could not determine whether charges were made to these 4 cards.
- There were often considerable delays in carrying out preventative maintenance work.
- There was no formal vehicle replacement policy and information on the deferred costs associated with maintaining vehicles beyond their economic lives was not known.
- There was no system to ensure vehicles are promptly disposed of.

## **Update on Prior Years' Report Items**

### **Update**

In June 1999, we asked the Department of Works, Services and Transportation to inform us as to the progress made on our 1997 recommendations. The Department's response to each of these recommendations is outlined below.

#### **Transportation Planning**

##### **1997 Recommendation**

*The transportation needs of the departments should be reviewed to determine the number and type of light vehicles required by Government.*

##### **Action Taken**

The Department indicated that they have commenced a review of all vehicles in the fleet to obtain information on each vehicle including the usage, type of usage, driver and driver job description. Since 1998-99, requests for replacement vehicles are assessed against the above information. Based on this data, requests have been altered by Fleet Management who have become more pro-active.

#### **Vehicle Acquisition**

##### **1997 Recommendations**

*The Department of Works, Services and Transportation should ensure that departments provide adequate documentation to justify vehicle acquisitions, including demonstrating that the type of vehicle requested is needed for a particular position(s), that the transportation need cannot be met by the department's existing fleet complement, and that alternatives to acquisition are considered.*

*Departments should clearly demonstrate the need for the type of vehicle being requested in relation to the required use.*

*The departments requesting approval for vehicle acquisitions should provide adequate documentation to demonstrate that, where appropriate, alternatives to acquisition were considered.*

*The Department should develop a reporting system that adequately records information on the costs of alternative methods of transportation.*

##### **Action Taken**

The Department indicated that effective for 1998-99, Fleet Management now require that all requests for vehicles for other than basic

## Update on Prior Years' Report Items

transportation have documentation justifying the type of vehicle requested. The Department also informed us that requests are monitored against previous vehicle usage to determine if past usage justifies having a vehicle. In addition, before a vehicle is purchased, a mechanical condition report is undertaken on the vehicle to be replaced and only those vehicles in poor mechanical condition are approved for replacement. As well, all requests for additions to the vehicle fleet must include a justification letter from the Department requiring the vehicle.

The Department also indicated that it does evaluations on all requests for rental of vehicles in excess of 30 days. To date, this is the only alternative in place for situations where low usage is estimated. For transportation needs of shorter durations, the individual department is required to find practical solutions.

The Department also informed us that while vehicle leasing is a popular alternative for the general public, it is not recommended as an alternative for most applications in the Government fleet. The Department cited the following reasons:

- Manufacturers' incentives are only available on normal vehicle purchases by Government;
- At the end of the lease, damages to vehicles may result in added costs; and
- Over a three year period, leasing costs are higher than the normal purchase option.

### Vehicle Operations

#### 1997 Recommendations

*The Department should ensure that the information necessary to manage Government's vehicle fleet is available.*

*Utilization and costs of operating Government's vehicle fleet should be adequately monitored and controlled.*

*The Department should ensure controls over the access to fuel at the Government-owned refueling sites are adequate.*

#### Action Taken

The Department indicated that the new on-line Equipment Management System (EMS) has eliminated many of the problems and concerns related

## **Update on Prior Years' Report Items**

to the previous batch information system. As a result, information is current, accurate and in a format that provides the necessary data to manage Government's vehicle fleet. In addition, the new system is access based and permits users to generate special reports, as required.

The Department also informed us that utilization and costs of operating each vehicle, vehicle type or class will be monitored in the new EMS. However, as the data base is new it does not yet contain sufficient information to identify trends to be used in decision making. It is expected that after several years of data collection, the system will produce more useful information.

In addition, the Department indicated that they have corrected the lack of controls over access to fuel at Government-owned refueling sites.

### **Vehicle Maintenance**

#### **1997 Recommendations**

*Departments should ensure that vehicles are maintained in accordance with Fleet Management policies and procedures.*

*The Department should ensure that the productivity levels at the depots are at an acceptable level.*

#### **Action Taken**

The Department indicated that it reviewed its Maintenance program and made numerous changes to have repairs and preventive maintenance completed in a more timely manner. Since 1998-99, Fleet Management has required that departments getting repairs done outside Government facilities forward documentation to Fleet Management so that it is recorded on the new EMS for that particular vehicle.

In addition, the Department informed us that the EMS records each mechanic's time on repair codes and that this information will be used to assess productivity for the facility and mechanics.

### **Vehicle Replacement**

#### **1997 Recommendation**

*The costs of maintaining vehicles beyond their economic lives should be determined for purposes of establishing a formal Government-wide replacement policy.*



## **Update on Prior Years' Report Items**

### **Action Taken**

The Department indicated that the new EMS will have a replacement module which will generate a listing of vehicles which should be considered for replacement. The vehicles identified on this listing will then undergo a complete mechanical assessment and a usage/needs analysis before a final decision regarding replacement is made.

With respect to maintaining vehicles beyond their economic lives, the Department informed us that the new EMS will compare the cost of repair against the current value of the vehicle.

### **Vehicle Disposition**

#### **1997 Recommendation**

*Fleet Management should monitor the timeliness of dispositions to ensure that this source of revenue is received as soon as possible. In addition, information systems should be promptly updated to reflect vehicle dispositions.*

### **Action Taken**

The Department indicated that vehicles are disposed of in a timely manner in the Avalon region due to the availability of auction services in this area. However, in other areas of the Province, the Department indicated that only annual auctions are held which produce higher disposal values and lower overhead costs.

## **4.2.9 Government Purchasing Agency *Public Tender Act* Exception Reporting (1997 Annual Report, Part 3.13)**

### **Introduction**

In 1997 we carried out a review at the Government Purchasing Agency to determine whether all public tender exceptions were tabled in the House of Assembly as required by the *Public Tender Act*. We also reviewed the system in place at the Government Purchasing Agency to determine whether it was recording all public tender exceptions.

As a result of our review we reported that the *Public Tender Act* required that, with few exceptions, all goods and services costing \$7,500 or more which had been acquired without public tender be reported to the House of Assembly. We found that although all exceptions that were reported to the Government Purchasing Agency were forwarded to the Minister of

## Update on Prior Years' Report Items

Works, Services and Transportation for tabling in the House of Assembly, the Government Purchasing Agency was not notified by government funded bodies of all exceptions. Therefore, the exception reports which were tabled in the House of Assembly were incomplete.

We reported that although the Act and Regulations required government funded bodies to report their public tender exceptions to the Minister of Works, Services and Transportation within five days of the awarding of the contract, our review disclosed that some exceptions were not reported by the government funded body until more than two years after the awarding of the contract.

We also reported that some of the reports which were tabled in the House of Assembly were not being tabled within the time frame specified in the Act.

We recommended that all government funded bodies comply with the *Public Tender Act* and the *Public Tender Regulations* and report all public tender exceptions to the Minister of Works, Services and Transportation within the period required by legislation. We also recommended that the Government Purchasing Agency ensure that it receives information relating to all public tender exceptions from all government funded bodies and that it review and challenge this information to ensure that it is complete, accurate and in compliance with legislation.

### Update

In June 1999, we asked the Department of Works, Services and Transportation to inform us as to the progress made on our 1997 recommendations relating to the Government Purchasing Agency- Public Tender Exception Reporting. In its response the Department indicated that due to fiscal restraint, unfortunately, the Government Purchasing Agency does not have sufficient human resources to perform compliance reviews on all government funded bodies to ensure exceptions are being recorded. The individual responsible for compiling the report to the House of Assembly reviews certain reports with government funded bodies, where required; however, due to time constraints this person is not able to challenge whether or not it is an exception. The onus for identifying exceptions rests with the government funded bodies and the Regulations of the *Public Tender Act* were changed to extend the notification period to 30 days from 5 days in order to allow sufficient time. In addition, Government Purchasing Agency officials continually provide information and training to government funded bodies in this regard. 4

## **Update on Prior Years' Report Items**

### **Department of Industry, Trade and Technology**

#### **4.2.10 The Economic Diversification and Growth Enterprises Act (1996 Annual Report, Part 3.3)**

##### **Introduction**

A Strategic Economic Plan for Newfoundland and Labrador was released in June 1992. It was indicated in the Plan that Government must create the proper economic and social environment for a competitive private sector. One initiative toward the creation of such an environment is the *Economic Diversification and Growth Enterprises Act* which became effective on 1 January 1995. Under this Act, the Economic Diversification and Growth Enterprises (EDGE) program provides significant tax incentives to new and expanding corporations that meet a number of qualifying criteria. The Act is administered by the Department of Industry, Trade and Technology.

The EDGE program is complimentary to other support and development programs currently available to businesses in the Province. The underlying objective of these programs is to make the Province one of the most attractive investment locations in North America. The intent of the EDGE legislation is to encourage private sector job creation and diversification of the provincial economy.

Corporations must apply to the Department for EDGE designation. Each application is evaluated by a board of public and private sector representatives which makes recommendations respecting the application to the Lieutenant-Governor in Council. The Board is currently comprised of six members, three of whom represent the private sector. The Department has stated that 161 EDGE applications had been received by the Department as at 30 October 1999. Cabinet has approved 67 of these applications. Of the remaining 94 applications, 59 have been rejected, 5 have been deferred and 30 others have had their EDGE status revoked. The corporations that meet the criteria are designated as EDGE Corporations.

The Department estimates that for the 67 applications approved, the EDGE program will create 3,549 permanent jobs through the investment of \$1.12 billion in capital.

In 1996, we conducted a review which provided for an examination of legislation and administrative procedures respecting the EDGE program. We made specific recommendations relating to the review of legislation, the compliance with legislation and the implementation of policies and procedures.

## **Update on Prior Years' Report Items**

### **Update**

The Department has taken some action on some of our outstanding recommendations as reported in our 1998 follow-up review; however, some still need to be addressed as outlined below:

#### **Review and Evaluation of the Act**

Although some amendments to the EDGE Act were assented to on 15 December 1998, the amendments do not address items in our recommendation regarding the review and evaluation of the Act. A consultants report to the Department in March 1997 stated that *"recommendations of the Auditor General in terms of review and evaluation of the Act should be implemented"*. The Department has provided no documented evidence that it performed a thorough review and evaluation of the Act as recommended.

#### **Compliance with the EDGE Act**

Our recommendation with regard to compliance with the EDGE Act was that the Department should comply with the Act. Our follow-up review last year indicated that while the Department had documented certain monitoring procedures to help ensure compliance with the Act, the procedures were not sufficiently detailed to ensure compliance with Sections 3 and 5 of the Act. Our follow-up review this year revealed that Section 5 of the Act was amended in December 1998 to remove a list of detailed requirements EDGE applicants were required to provide. These information requirements are now included in a procedures manual. The Department has prepared a checklist to ensure the basic program criteria in Section 3 have been satisfied.

#### **Administration of the EDGE Program**

Our recommendation respecting EDGE application receipt, evaluation and approval was that procedures should be implemented to ensure all information is received and guidelines should be established to ensure all applications are evaluated on a consistent basis. Our current review of documented procedures regarding the receipt and evaluation of information under Section 3 of the Act indicated that a checklist has been implemented to ensure basic program criteria have been satisfied. In addition, the procedures manual includes a list of information required to be included in a business plan. The procedures manual does not address our concerns for consistent evaluation in areas such as what constitutes, per Section 3, a *"substantial net economic benefit to the Province"* and that the venture was undertaken due to EDGE incentives.



## **Update on Prior Years' Report Items**

### **4.2.11 The Privatization of Newfoundland Hardwoods Limited (1997 Annual Report, Part 3.16)**

#### **Introduction**

In our 1996 Annual Report to the House of Assembly, we reported on the results of our review of the privatization of Newfoundland Hardwoods Limited (the Corporation). This review disclosed that although the assets of the Corporation were sold in August and September 1995, as of October 1996, the transactions had yet to be finalized, audited financial statements for the year ended 31 March 1996 had not been released, and the Province had only received \$5.6 million of the \$7.0 million in proceeds.

In our 1997 Annual Report to the House of Assembly, we again reported that the issues noted in the previous paragraph were still outstanding.

In 1998 we completed and reported on a follow up review of the privatization of Newfoundland Hardwoods Limited. This review disclosed that audited financial statements had been completed to 31 March 1998; however, there were still issues regarding the wind-up of the pension plan and the removal of storage tanks.

#### **Update**

For the fiscal year ended 31 March 1999 Newfoundland Hardwoods Limited recorded revenues of \$134,000 from gain on wind-up of pension plan, interest and miscellaneous. The Corporation had approximately \$776,000 in its bank account and owed \$54,000 to creditors. The Department has indicated that tenders will be called for the removal of the storage tanks and once this is completed, the Corporation will be wound up.

## **Department of Health and Community Services**

### **4.2.12 Faculty of Medicine of Memorial University of Newfoundland (1997 Annual Report, Part 3.19)**

#### **Introduction**

In 1997, we performed a review to determine whether the Department of Health had an adequate system of accountability over the grants provided to the Faculty of Medicine.

We concluded that the Department of Health did not have an adequate system of accountability over the grants provided to the Faculty of Medicine. More specifically, the Department was not requesting sufficient information to determine whether the Faculty was effectively spending operating grants for the intended purposes. Such information would include interim and annual audited financial information, and information on program objectives and accomplishments. In addition, we concluded

## Update on Prior Years' Report Items

that the Department had not performed any audits of the Faculty's operations to assess the adequacy of management systems and controls and compliance with authorities.

### Update

In June and September of 1999, we contacted the Department to determine if any action had been taken on our 1997 recommendations. The Department's response to each of these recommendations is outlined below.

#### 1997 Recommendations

*The Department should establish a system of accountability over grants paid to the Faculty of Medicine. This system would include adequate reporting to the Department and the House of Assembly on both the financial and operational performance of the Faculty.*

*The Department should perform periodic audits of the Faculty's operations.*

#### Action Taken

The Department agrees that an acceptable level of accountability should be obtained through financial and operational reporting. The Department indicates that it requests an annual detailed budget submission, identifying various components of the budget, for both the Undergraduate and the Postgraduate programs. The Department indicated that it meets with officials to review these budget submissions. For the Undergraduate Program the Department reported that as part of the 1999-2000 budget submission, the following information was received:

- 1998-1999 approved budget and year to date actuals showing all cost centres;
- 1999-2000 budget request identifying and explaining variances between the 1998-1999 approved budget and the 1999-2000 budget request; and
- comparative analysis of expenditures from 1991-1992 to 1998-1999 and projected expenditures for 1999-2000.

The Department indicated that, in future, it will also request quarterly financial reports to monitor budget to actual. For the Postgraduate Program, the Department reported that it received the budget submission for the Health Care Corporation, which includes a specific functional centre for the Postgraduate Program.



## **Update on Prior Years' Report Items**

With respect to the recommendation on periodic audits, the Department indicated that it has made some effort to conduct a financial and operational review of the programs administered by the Faculty of Medicine; however, other Departmental matters took precedence and the review was postponed. The Department indicated that it has recently implemented a major restructuring and has received approval to create a separate audit section within the Financial Services Division which is responsible for auditing Government funded boards and agencies. The Department, in developing its audit plan, will be reassessing the timing and scope of a financial and operational review of the Faculty of Medicine's Undergraduate and Postgraduate Programs.

## **Update on Prior Years' Report Items**

CHAPTER

5

GENERAL MATTERS AND WORK OF  
THE AUDIT OFFICE



## CHAPTER

### 5

## General Matters and Work of the Audit Office

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## General Matters and Work of the Audit Office

### 5.1 Operations of the Office of the Auditor General

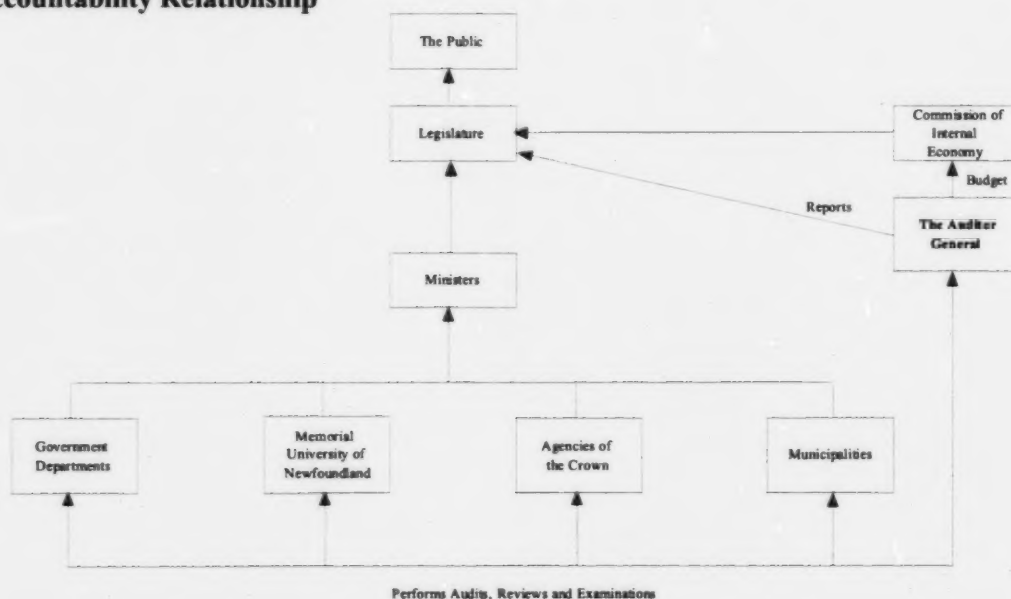
#### Mandate and Objectives

The Office of the Auditor General operates under the authority of the *Auditor General Act* which was assented to 31 October 1991. The full text of the *Auditor General Act* is presented as Appendix I to this Report. The Auditor General is appointed for a 10 year non-renewable term as an officer of the House of Assembly and is the independent Legislative Auditor of Government, its departments, all Crown agencies and Memorial University of Newfoundland. Implicit in the *Auditor General Act* is the requirement for the Auditor General to provide the House of Assembly with timely, relevant information, necessary to enhance public sector accountability and performance.

Public sector accountability is based on the premise that governing bodies are best served by knowing whether the responsibilities conferred on government departments and agencies are satisfactorily performed and intended results are achieved. The Auditor General brings an independent audit process to the manner in which these conferred responsibilities are discharged in the public sector and reports directly to the House of Assembly on the results of these audits. The role of the Auditor General complements the accountability relationship which exists between Government, its departments, agencies of the Crown, Memorial University of Newfoundland, municipalities, and the House of Assembly, as illustrated in Figure 1.

Figure 1

#### Office of the Auditor General Accountability Relationship





## General Matters and Work of the Audit Office

### Reports

The Auditor General reports to the House of Assembly on significant matters which result from the examinations of Government, its departments and agencies of the Crown and Crown controlled corporations.

Our process for conducting examinations provides senior officials with an opportunity to meet and discuss the scope and objectives of our work before it commences. Furthermore, every report resulting from our examinations includes our conclusions, findings and recommendations and is reviewed with senior officials before being included in the Annual Report to the House of Assembly. This validation process allows the senior officials the opportunity to provide any new or additional information that may not have been previously provided.

The Auditor General is also the independent auditor of the Province's financial statements and the financial statements of many agencies of the Crown and, as such, expresses an opinion on these financial statements.

A list of Departmental audits performed by our Office is included as Appendix II of this Report. A list of agencies of the Crown and other entities whose financial statement audits are performed by our Office is included as Appendix III of this Report. A list of agencies of the Crown and other entities whose financial statement audits are performed by private sector auditors is included as Appendix IV of this Report.

Section 12 of the *Auditor General Act* requires the Auditor General to report on:

- the work of the office;
- whether, in carrying out the work of the office, the Auditor General received all the information including reports and explanations required;
- the results of the examination of the Province's financial statements;
- audits, examinations and inquiries performed under the Act; and
- the results of the examination of the accounts of the Province calling attention to anything the Auditor General considers significant relating to:
  - collections of public money;
  - disbursements of public money;

## General Matters and Work of the Audit Office

- whether accounts have not been faithfully and properly kept;
- whether assets acquired, administered or otherwise held are not adequately safeguarded or accounted for;
- whether accounting systems and management control systems that relate to revenue, disbursements, the safeguarding or use of assets or the determination of liabilities were not in existence, were inadequate or had not been complied with; and
- any factors or circumstances relating to an expenditure of public money which in the opinion of the Auditor General should be brought to the attention of the House of Assembly.

## Mission and Values

The Office of the Auditor General initiated a strategic planning process in August 1994 and completed its first Strategic Plan in June 1995. The Plan was updated in 1996 and again in 1999 and now focuses on the priorities and initiatives of the Office to 2002. The strategic planning process required the development of an office mission statement and identification of our values as follows:

### Mission Statement

*The Office of the Auditor General serves the House of Assembly by providing independent examinations of Government and its entities.*

*As legislative auditors, we audit financial statements and other accountability documents, evaluate management practices and control systems, and determine compliance with legislative and other authorities.*

*Our purpose is to promote accountability and encourage positive change in the stewardship, management and use of public resources.*

### Values

We believe in independence for our Office, integrity in our conduct and quality in our work. Therefore we will:

*Maintain our independence and avoid the perception of bias;*

*Strive for excellence in our work and seek continuous improvement in our use of technology, methodology and training;*

## **General Matters and Work of the Audit Office**

*Treat all external parties with courtesy and respect; and*

*Conduct ourselves according to the highest professional standards.*

We believe everyone should be treated with fairness and respect. Therefore, in our Office, all employees:

*Are recognized and valued for contributions;*

*Communicate openly and work together as a team;*

*Receive necessary opportunities for professional and personal growth; and*

*Are accountable for quality performance and encouraged to improve processes.*

## **Our Work**

The development of our Strategic Plan resulted in the identification of five main lines of business which serve as a means of determining priorities and allocating resources. The Plan also resulted in the establishment of goals that we now use to measure our progress. The five lines of business, related goals and results to date are outlined as follows:

### **1. Financial Statement Audits**

A financial statement audit enables the Auditor General to express an opinion as to whether the financial statements present fairly the subject matter with which they deal. The opinion is based on an independent assessment and therefore adds credibility to the information to which it is attached.

#### **Goal 1.1**

To complete all financial statement audits by the established deadlines.

#### **Status**

All financial statements presented for audit as required were completed by the established deadlines. There were, however, seven entities whose financial statements, because of late submission to our Office, were not completed by the established deadline.

Appendices III and IV indicate the audits completed by the Auditor General and the private sector auditors respectively, their fiscal year ends and the date of the Auditor's Report.

## **General Matters and Work of the Audit Office**

### **Goal 1.2**

To assess the time budget for each area of each financial statement audit to determine whether audit procedures can be reduced or eliminated.

#### **Status**

At the conclusion of each financial statement audit each audit time summary is reviewed in detail and compared with the original time budget. Prior to the commencement of the following year's audit, as part of the planning phase, the time budget is reviewed to determine whether there are areas where the audit time can be reduced. While improvements have been made in this area, we are continually trying to become more efficient.

### **Goal 1.3**

To complete all financial statement audits within a 10% variance of budget for time and cost.

#### **Status**

The majority of financial statement audits were completed within a 10% variance of budget for time and cost. Any variations were caused by the particular circumstances associated with the entities being audited.

### **Goal 1.4**

To have 100% compliance with professional standards and internal Office policy for all audits.

#### **Status**

All financial statement audits were conducted in accordance with professional standards and internal Office policy.

## **2. Legislative Audits**

Legislative audits provide the House of Assembly with an independent professional assessment of public sector accountability, thereby facilitating informed judgements on the manner in which the public sector discharges its responsibilities. Legislative audits may include evaluation of accountability relationships, management practices and control systems; assessment of compliance with legislation and other authorities; and performance audits of program results compared to established criteria.

## **General Matters and Work of the Audit Office**

### **Goal 2.1**

To further develop our risk based management system. We will apply this system to our Office's audit universe each year to select audit projects.

#### **Status**

The computerized risk based audit management system was developed in the spring of 1997 and has been used in planning for all audit cycles each year since then.

### **Goal 2.2**

To provide the House of Assembly with an annual accountability document on the Office of the Auditor General.

#### **Status**

Chapter 5 of this Report provides the accountability report on the Office for the 1998-99 year. This includes the financial statements of the Office and a report on the goals of the Office along with their status at report date.

### **Goal 2.3**

To have 80% of our recommendations implemented within 2 years of our report date.

#### **Status**

In 1996 we established a system to measure the extent to which Government implements our recommendations. It is our intention to monitor and update the recommendations in each Annual Report two years after it has been issued. Monitoring will continue until we are reasonably satisfied that the issues are being adequately addressed or are no longer valid.

Overall for the four years from 1994 to 1997, satisfactory progress has been made on 81% of our recommendations or the recommendations are no longer applicable. The percentages for each year are 1994 (76%), 1995 (83%), 1996 (88%) and 1997 (78%).

### **Goal 2.4**

To have all reports subjected to quality control criteria and a challenge review process.



## **General Matters and Work of the Audit Office**

### **Status**

All legislative reports are subject to quality control criteria and a formal challenge review process.

### **3. Monitoring Crown Agency Reports**

Our role is to assess all of these entities over an appropriate number of years and to report on their accountability, management practices and control systems, their compliance with legislation, their performance related to established criteria, and any weaknesses or other issues which we feel should be brought to the attention of the House of Assembly.

#### **Goal 3.1**

To monitor Crown agency financial statements and other reports throughout the year using a computerized database to maintain the results.

#### **Status**

We have developed and are using a database system to maintain the financial statements, reports and other information of all agencies of the Crown.

#### **Goal 3.2**

To report on the monitoring of Crown agency financial statements and other reports to the House of Assembly on an annual basis.

#### **Status**

Part 3.1 of this Report contains the results of this work.

### **4. Special Assignments**

Under section 16 of the *Auditor General Act*, the Auditor General may accept assignments from the House of Assembly, the Public Accounts Committee and the Lieutenant-Governor in Council. The results of these assignments are reported to the body making the request.

#### **Goal 4.1**

To perform and report on special assignments whenever requested by the House of Assembly, Public Accounts Committee or the Lieutenant-Governor in Council.



## **General Matters and Work of the Audit Office**

### **Status**

While we have completed a number of special assignments in recent years, there were no special assignments during the 1998-99 fiscal year.

### **Goal 4.2**

To report on all special assignments conducted within six months of beginning our work.

### **Status**

There were no special assignments during the 1998-99 fiscal year.

### **Goal 4.3**

To subject all special assignment reports to quality control criteria and a challenge review process.

### **Status**

While there have been no special assignments during the 1998-99 fiscal year, our quality control and challenge review process requires that all audits, reviews, or assignments be subject to quality control criteria and a formal challenge review process.

## **5. Reporting**

The *Auditor General Act* requires that we report, at least annually, to the House of Assembly on the results of our examination of the Province's financial statements and on the results of any audits, examinations or inquiries which we have performed. In addition, when we have completed a financial statement audit we attach our auditor's report to the financial statements and issue a management letter to the entity examined. When we perform a legislative audit, we issue a management report which includes the entity's response to any comments made.

### **Goal 5.1**

To report on legislative audits in November of each year. To report on the financial statements of the Province and the monitoring of Crown agencies each November.

## General Matters and Work of the Audit Office

### Status

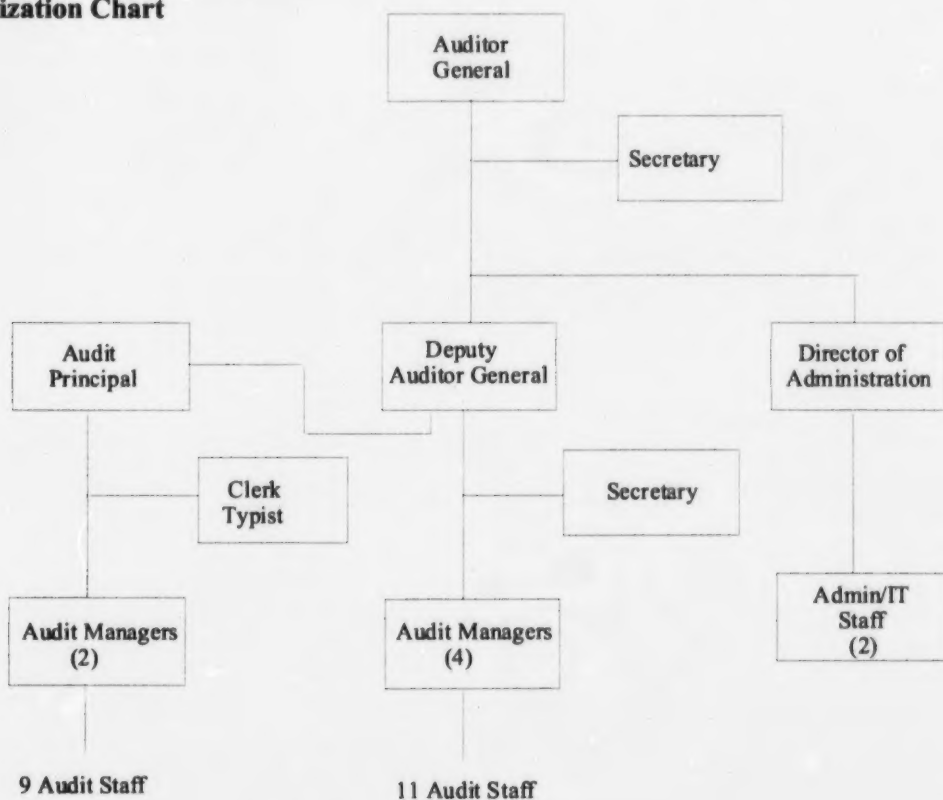
Our 1998 Report was tabled in December 1998. When the House of Assembly adjourned on 14 December 1999 this (our 1999) Report had not been presented to the Speaker for tabling in the House of Assembly. It was presented to the Speaker on 31 January 2000 and will be tabled in the House of Assembly when it reopens. This Report and my Report on the Audit of the Financial Statements of the Province which accompanies it contain our comments on legislative audits and the audit of the financial statements of the Province for the year ended 31 March 1999.

### Organization

Our employees are our most valuable resource because it is their knowledge and skill that determine the quality of the work that is performed. The Office is organized to allow for the efficient and effective deployment of staff and to support our work. The organizational structure of the Office is outlined in Figure 2.

Figure 2

#### Office of the Auditor General Organization Chart



## General Matters and Work of the Audit Office

There are three support services in the Office with the following responsibilities:

*Administration* - provides strategic and policy advice on human resource management, financial management and report publishing initiatives. At the operational level, this area also provides such services as recruitment, payroll, secretarial support, file registry and purchasing.

*Professional Practice* - provides technical advice on accounting and auditing policy and practice matters. This area reviews current and emerging accounting and auditing issues within the public sector and provides comments to professional bodies and central agencies.

*Information Technology* - provides consultation and technical support on all matters dealing with information technology. This area is responsible for implementation of the Office's information technology strategic plan. It also monitors technological developments relevant to the Office, provides ongoing operational support and assists in training activities.

The Office had 35 employees as of 30 November 1999, 31 in the St. John's Office and 4 in the Corner Brook Office. Of the 35 employees, 22 have professional accounting designations and 7 are in the process of completing their professional accounting program. Figure 3 indicates the Auditor General and the staff of the Office as at 30 November 1999.

**Figure 3**

### Office Staff 30 November 1999

|                                                                                                                                                                                                        |                                                                                                                                                                                                                               |                                                                                                                                                                                                           |                                |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------|
| Kevin Antle CGA<br>Paul Burggraaf<br>Keith Butt CA<br>John Casey CMA<br>Rosemarie Crann<br>Gertrude Critch<br>Lisa Crowley CA<br>Tony Dingwell CA<br>Bill Drover FCA<br>James Foran<br>Kerry Griffiths | Martin Hattenhauer CA<br>Claude Janes CA<br>Brenda Kavanagh<br>Nancy King<br>Wayne Loveys CMA<br>James Mallard CGA<br>Elizabeth Marshall CA<br>Trevor McCormick CGA<br>Julia Mullaley CA<br>Bill Nofall<br>John Noseworthy CA | Steve Pearce<br>Tracy Pelley CMA<br>Deann Penney<br>David Pike<br>David Ralph CA<br>Tony Roestenberg CA<br>Sandra Russell CA<br>Denise Tubrett CGA<br>Paul Tucker<br>Scott Walters CA<br>David White FCGA | Jim Winsor CMA<br>Tony Wiseman |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------|

## **General Matters and Work of the Audit Office**

### **Professional Development and Training**

A program of ongoing training and professional development of staff is essential to ensure that staff keep current with new auditing techniques used in the profession. This program consists of on-the-job training, external and in-house courses, and seminars.

We continue to encourage our staff to pursue and complete programs of study which enable them to obtain professional accounting designations. We are pleased to note that during the year the following members of our staff obtained their professional accounting designation.

- Lisa Crowley, CA; and
- Trevor McCormick, CGA

We wish continued success to the seven members of our staff who are now studying towards a professional accounting designation.

We are also pleased to note that David White, FCGA received his fellowship from the Certified General Accountants Association of Canada.

### **Financial Statements**

The gross expenditures of the Office totalling \$2,157,297 for the year ended 31 March 1999 were within the limits of the approved budget. The following financial statements were audited by a public accounting firm.

## **General Matters and Work of the Audit Office**

### **AUDITOR'S REPORT**

To the Commission of Internal Economy  
House of Assembly  
Province of Newfoundland

I have audited the schedule of assets and liabilities of the Office of the Auditor General, Province of Newfoundland as at 31 March 1999 and the statement of expenditure and related revenue for the year then ended. This financial information is the responsibility of the Office's management. My responsibility is to express an opinion on this financial information based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial information is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial information. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial information.

In my opinion, this financial information presents fairly, in all material respects, the financial position of the Office as at 31 March 1999 and the results of its operations for the year then ended, in accordance with the accounting principles disclosed in Note 1 to the financial information.

**BERNARD P. HOGAN**  
**CHARTERED ACCOUNTANT**

St. John's, Newfoundland  
November 3, 1999

## General Matters and Work of the Audit Office

### OFFICE OF THE AUDITOR GENERAL PROVINCE OF NEWFOUNDLAND SCHEDULE OF ASSETS AND LIABILITIES 31 MARCH 1999

|                                   | <u>1999</u>       | <u>1998</u>      |
|-----------------------------------|-------------------|------------------|
| <b>ASSETS</b>                     |                   |                  |
| <b>Current</b>                    |                   |                  |
| Audit fees billed and in progress | \$ 103,362        | \$ 85,144        |
| Travel imprests                   | 1,200             | 1,400            |
| Accountable advance               | <u>200</u>        | <u>200</u>       |
|                                   | <u>\$ 104,762</u> | <u>\$ 86,744</u> |
| <b>LIABILITIES</b>                |                   |                  |
| <b>Current</b>                    |                   |                  |
| Accrued leave                     | \$247,432         | \$203,516        |
| Vouchers/HST payable              | 13,803            | 11,391           |
| Accrued payroll                   | 5,995             | 62,194           |
| Accrued severance pay             | <u>338,721</u>    | <u>309,476</u>   |
|                                   | <u>\$605,951</u>  | <u>\$586,577</u> |

*See accompanying notes*

Signed on behalf of the Office: \_\_\_\_\_  
Auditor General of Newfoundland



# General Matters and Work of the Audit Office

## OFFICE OF THE AUDITOR GENERAL PROVINCE OF NEWFOUNDLAND STATEMENT OF EXPENDITURE AND RELATED REVENUE FOR THE YEAR ENDED 31 MARCH 1999

|                                     | <u>Estimates</u>   |                    |                    |
|-------------------------------------|--------------------|--------------------|--------------------|
|                                     | Actual             | Amended            | Original           |
| <b>EXECUTIVE SUPPORT</b>            |                    |                    |                    |
| Salaries                            | \$ 117,143         | \$ 117,740         | \$ 118,440         |
| Salaries (statutory)                | 99,260             | 99,260             | 99,260             |
| Employee benefits                   | 3,262              | 3,800              | 4,800              |
| Transportation and communications   | 16,875             | 17,000             | 17,000             |
| Professional services               | 5,087              | 5,200              | 20,000             |
| Purchased services                  | <u>666</u>         | <u>700</u>         | <u>700</u>         |
|                                     | <u>242,293</u>     | <u>243,700</u>     | <u>260,200</u>     |
| <b>ADMINISTRATIVE SUPPORT</b>       |                    |                    |                    |
| Salaries                            | 188,126            | 188,200            | 174,400            |
| Employee benefits                   | 621                | 700                | 3,400              |
| Transportation and communications   | 30,817             | 30,900             | 28,200             |
| Supplies                            | 19,974             | 21,000             | 17,100             |
| Purchased services                  | 159,265            | 160,300            | 147,300            |
| Property, furnishings and equipment | 11,439             | 11,500             | 3,000              |
| Grants and subsidies                | <u>5,000</u>       | <u>5,000</u>       | <u>5,000</u>       |
|                                     | <u>415,242</u>     | <u>417,600</u>     | <u>378,400</u>     |
| <b>AUDIT OPERATIONS</b>             |                    |                    |                    |
| Salaries                            | 1,270,653          | 1,270,900          | 1,310,300          |
| Employee benefits                   | 11,626             | 13,000             | 10,000             |
| Transportation and communications   | 53,693             | 54,500             | 49,500             |
| Professional services               | 10,281             | 10,500             | 15,000             |
| Information technology              | <u>153,509</u>     | <u>155,000</u>     | <u>141,800</u>     |
|                                     | <u>1,499,762</u>   | <u>1,503,900</u>   | <u>1,526,600</u>   |
| Revenue - provincial                | <u>(122,177)</u>   | <u>(157,800)</u>   | <u>(157,800)</u>   |
|                                     | <u>1,377,585</u>   | <u>1,346,100</u>   | <u>1,368,800</u>   |
| Net Expenditure                     | <u>\$2,035,120</u> | <u>\$2,007,400</u> | <u>\$2,007,400</u> |

See accompanying notes

## General Matters and Work of the Audit Office

### OFFICE OF THE AUDITOR GENERAL PROVINCE OF NEWFOUNDLAND STATEMENT OF GROSS EXPENDITURE AND UNEXPENDED BALANCES FOR THE YEAR ENDED 31 MARCH 1999

|                                                                    |                  |
|--------------------------------------------------------------------|------------------|
| Original estimates (net)                                           | \$2,007,400      |
| Add back revenue estimates net of transfers and statutory payments | <u>58,540</u>    |
| Original estimates of expenditure                                  | 2,065,940        |
| Supplementary supply                                               | <u>-</u>         |
| Total appropriation                                                | <u>2,065,940</u> |
| Total net expenditure                                              | 2,035,120        |
| Add revenue less transfers and statutory payments                  | <u>22,917</u>    |
| Total gross expenditure (budgetary, non-statutory)                 | <u>2,058,037</u> |
| Unexpended balances of appropriation                               | <u>\$ 7,903</u>  |

#### Summary of Cash Payments and Receipts

|                 | <u>Payments</u>    | <u>Receipts</u>   | <u>Net</u>         |
|-----------------|--------------------|-------------------|--------------------|
| Current Account | <u>\$2,157,297</u> | <u>\$ 122,177</u> | <u>\$2,035,120</u> |

## General Matters and Work of the Audit Office

### OFFICE OF THE AUDITOR GENERAL PROVINCE OF NEWFOUNDLAND NOTES TO FINANCIAL INFORMATION 31 MARCH 1999

#### Authority

Section 3 of the *Auditor General Act* provides for the establishment of a department of the public service of the province called the Office of the Auditor General. This Act was assented to on 31 October 1991. The Act provides for the annual audit of the Office and requires that the auditor submit his or her report to the Commission of Internal Economy for tabling before the House of Assembly.

#### 1. Significant accounting policies

This financial information has been prepared by the Office of the Auditor General on a cash basis of accounting modified in accordance with the *Financial Administration Act*. Outlined below are the significant policies followed:

(a) Revenues

Revenues are recorded when actually received.

(b) Expenditures

Expenditures are recorded when actually paid except that liabilities incurred for the financial year ended 31 March, invoices for which are received by the Comptroller General by 30 April, are recorded as if they were paid by 31 March.

(c) Assets and liabilities

Assets and liabilities are recorded on a basis consistent with the policies used in preparing the Public Accounts of the Province of Newfoundland. Direct liabilities and convertible assets such as amounts receivable are reported in the Schedule of Assets and Liabilities.

(d) Inventories

Inventories are not considered to be convertible and therefore are not valued in the Schedule of Assets and Liabilities. They are charged as budgetary expenditures and are expensed in the year they are acquired.

## **General Matters and Work of the Audit Office**

### **OFFICE OF THE AUDITOR GENERAL PROVINCE OF NEWFOUNDLAND NOTES TO FINANCIAL INFORMATION 31 MARCH 1999**

#### **1. Significant accounting policies (cont.)**

**(e) Operating expenses**

The employer's portion of government personnel costs is paid by the Department of Finance and is not reflected in this financial information.

**(f) Fixed assets**

Fixed asset acquisitions are charged as budgetary expenditures and are expensed in the year they are acquired. The assets are not considered to be convertible and therefore are not capitalized and are not valued on the Schedule of Assets and Liabilities.

**(g) Income taxes**

The Office of the Auditor General is not subject to Provincial or Federal income taxes.

#### **2. Pensions**

Under the *Auditor General Act*, all persons employed in the Office of the Auditor General are employees for the purposes of the *Public Service Pensions Act, 1991*, and are entitled to all the benefits under that Act. No pension expenditure has been recorded in this financial information.

## **General Matters and Work of the Audit Office**

### **5.2 Special Reports**

#### **Reports under Section 15 of the *Auditor General Act***

##### **Department of Education**

Section 15 of the *Auditor General Act* requires that we report to the Lieutenant-Governor in Council any improper retention or misappropriation of public money or other activity that comes to our attention during our audits. This section also requires that we provide a general description in the Auditor General's annual report of any incidents referred to the Lieutenant-Governor in Council.

On 11 February 1999 we reported to the Lieutenant-Governor in Council that our review of travel expenditures of the Department of Education disclosed inappropriate travel claims made by a senior employee.

## **General Matters and Work of the Audit Office**



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## APPENDICES

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# APPENDICES

|                                                                                                                             |     |
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## Appendix I

1. This Act may be cited as the *Auditor General Act*.
2. (1) In this Act
  - (a) "agency of the Crown" means an authority, board, commission, foundation, agency, corporation, association, institute or other body of persons, whether incorporated or unincorporated, 50% or more of the members of which or 50% or more of the members of the board of management or board of directors of which,
    - (i) are appointed by an Act of the Legislature or by the Lieutenant-Governor in Council, or
    - (ii) where not so appointed, in the discharge of their duties are public officers or servants of the Crown or are responsible to the Crown for the proper discharge of their duties;
  - (b) "audit" means an audit or examination of accounts of public money that may be made by the auditor general under this Act;
  - (c) "auditor general" means the Auditor General of Newfoundland appointed under section 4;
  - (d) "commission" means the Commission of Internal Economy of the House of Assembly appointed under the authority of *The Internal Economy Commission Act*;
  - (e) "Crown controlled corporation" means a corporation that is not an agency of the Crown and having
    - (i) 50% or more of its issued and outstanding shares vested in the Crown or in the name of a minister of the Crown, or
    - (ii) the appointment of a majority of its board of directors made or approved by the Lieutenant-Governor in Council;
  - (f) "office" means the Office of the Auditor General established under section 3; and
  - (g) "public money" means all money received, held or collected for or on behalf of the province by a minister of the Crown or other public officer in his or her official capacity or by a person authorized to receive, hold or collect that money, and includes
    - (i) all revenues of the province,
    - (ii) money borrowed by the province or received through the issue and sale of securities, and
    - (iii) money paid to the province for a special purpose.

## Appendix I

(2) Words and expressions used in this Act and not defined in subsection (1) have the same meaning as in *The Financial Administration Act, 1973*.

3. There is established a department of the public service of the province called the Office of the Auditor General, over which the auditor general shall preside.

4. (1) The Lieutenant-Governor in Council shall, by commission under the Great Seal of the province, appoint a qualified auditor to be the officer called the Auditor General of Newfoundland.

(2) The person appointed to the position of auditor general under this section must be confirmed in office as auditor general by the introduction in the House of Assembly of a resolution within 10 days after his or her appointment and if the House of Assembly is not sitting within 10 days after the commencement of the next ensuing Session of the House of Assembly or within 10 days after the House of Assembly resumes sitting following an adjournment of the House of Assembly.

(3) The auditor general is by virtue of his or her position an officer of the House of Assembly.

5. (1) The auditor general holds office for a term of 10 years but may be removed for cause by the Lieutenant-Governor in Council following the passing by the House of Assembly of a resolution requesting the Lieutenant-Governor in Council to do so.

(2) Once having served as auditor general, a person is not eligible for reappointment to that office.

6. In the event of the absence or incapacity of the auditor general or where the Office of Auditor General is vacant, the Lieutenant-Governor in Council may appoint a person temporarily to perform the duties of the auditor general.

7. The auditor general shall be paid a salary out of the Consolidated Revenue Fund at a rate set by the Lieutenant-Governor in Council and is entitled to the privileges of office of a deputy minister.

8. The auditor general shall not hold an office of profit or shall not act as trustee for profit for another person, other than his or her office as auditor general or engage in an occupation for reward outside the duties of his or her office.

9. (1) Before entering upon his or her duties, the auditor general shall

(a) take or make and sign the Oath or Affirmation of Allegiance under *The Oaths of Office Act*; and

(b) take or make and sign the following oath or affirmation of office:

"I, ....., do solemnly swear (or solemnly, sincerely and truly declare and affirm) that I will faithfully, truly, impartially, honestly, justly and to the best of my judgment, skill and ability, execute and perform the powers, duties and functions reposed in or required of me as auditor general under the *Auditor General Act* or another Act and that I will observe and comply with the laws of Canada and Newfoundland." (Where an oath is taken add "So help me God").

## Appendix I

(2) The oaths or affirmations referred to in subsection (1) shall be administered by the Speaker or by the Clerk of the House of Assembly.

10. The auditor general is the auditor of the financial statements and accounts of the province and shall make those examinations and inquiries that the auditor general considers necessary to enable him or her to report as required by this Act.

11. The auditor general shall examine the several financial statements required by *The Financial Administration Act, 1973* to be included in the public accounts of the province, and any other statement that is required to be audited by the auditor general under that Act or another statement that the Minister of Finance may present for audit and shall express his or her opinion as to whether the financial statements present fairly the financial position, results of operations and changes in the financial position of the province in accordance with the disclosed accounting policies of the provincial government and on a basis consistent with that of the preceding year, together with reservations the auditor general may have.

12. (1) The auditor general shall as he or she considers necessary but at least annually report to the House of Assembly on

- (a) the work of the office;
- (b) whether, in carrying out the work of the office, the auditor general received all the information including reports and explanations the auditor general required;
- (c) the results of the auditor general's examination of the financial statements referred to in section 11; and
- (d) audits, examinations and inquiries performed under this Act.

(2) A report of the auditor general under subsection (1) shall include the results of the auditor general's examination of the accounts of the province, and shall call attention to anything the auditor general considers significant, including instances where

- (a) collections of public money
  - (i) have not been effected as required under various Acts and regulations, directives or orders under those Acts,
  - (ii) have not been fully accounted for, or
  - (iii) have not been properly reflected in the accounts;
- (b) disbursements of public money
  - (i) have not been made in accordance with the authority of a supply vote, or relevant Act,
  - (ii) have not complied with regulations, directives or orders applicable to those disbursements,



## Appendix I

- (iii) have not been properly reflected in the accounts, or
    - (iv) have not been made for the purposes for which it was appropriated;
  - (c) accounts have not been faithfully and properly kept;
  - (d) assets acquired, administered or otherwise held are not adequately safeguarded or accounted for;
  - (e) accounting systems and management control systems that relate to revenue, disbursements, the safeguarding or use of assets or the determination of liabilities were not in existence, were inadequate or had not been complied with; or
  - (f) factors or circumstances relating to an expenditure of public money which in the opinion of the auditor general should be brought to the attention of the House of Assembly.
- (3) Paragraph (2)(f) shall not be construed as entitling the auditor general to question the merits of policy objectives of the government.
13. (1) Each report of the auditor general referred to in section 12 shall be submitted to the Speaker of the House of Assembly and the Speaker shall table each report before the House of Assembly immediately after receipt of the report by him or her or, where the House of Assembly is not then in Session, on the 1st day of the commencement of the next ensuing Session of the House of Assembly or on the 1st day after the House of Assembly resumes sitting following an adjournment of the House of Assembly.
- (2) The annual report of the auditor general shall be submitted on or before January 31 following the close of the fiscal year to which the report relates.
14. (1) Where an auditor has not been appointed to audit an agency of the Crown or a Crown controlled corporation, the auditor general shall be the auditor.
- (2) Where the auditor of an agency of the Crown or of a Crown controlled corporation is other than the auditor general, the auditor shall
- (a) deliver to the auditor general after completion of the audit a copy of the auditor's report, his or her recommendations to management and a copy of the audited financial statements of the corporation or agency;
  - (b) make available immediately to the auditor general, when so requested by the auditor general, all working papers, reports, schedules and other documents in respect of the audit; and
  - (c) provide immediately to the auditor general, when so requested by the auditor general, a full explanation of work performed, tests and examinations made and the results obtained, and other information relating to the audit within the knowledge of that auditor in respect of the agency or corporation.

## Appendix I

(3) Where the auditor general is of the opinion that the information, explanation or document that is provided, made available or delivered to the auditor general by the auditor referred to in subsection (2) is insufficient to permit the auditor general to exercise his or her powers or duties under this Act, the auditor general may conduct or cause to be conducted an additional examination and investigation of the records and operations of the agency of the Crown or the Crown controlled corporation that the auditor general considers necessary.

15. (1) Where during the course of an audit, the auditor general becomes aware of an improper retention or misappropriation of public money or another activity that may constitute an offence under the *Criminal Code* or another Act, the auditor general shall immediately report the improper retention or misappropriation of public money or other activity to the Lieutenant-Governor in Council.

(2) In addition to reporting to the Lieutenant-Governor in Council under subsection (1), the auditor general shall attach to his or her annual report to the House of Assembly a list containing a general description of the incidents referred to in subsection (1) and the dates on which those incidents were reported to the Lieutenant-Governor in Council.

16. (1) The auditor general may, where in his or her opinion such an assignment does not interfere with the auditor general's primary responsibilities under this Act, whenever the Lieutenant-Governor in Council so requests or the House of Assembly or the Public Accounts Committee by resolution so requires, inquire into and report on a matter relating to the financial affairs of the province or to public property or inquire into and report on a person or organization that has received financial aid from the government of the province or in respect of which financial aid from the government of the province is sought.

(2) Where the auditor general makes a report in accordance with subsection (1), the auditor general shall report back to either the Lieutenant-Governor in Council, the House of Assembly or the Public Accounts Committee.

17. Except as provided by another Act that expressly refers to this section, every department of government, every agency of the Crown and every Crown controlled corporation shall furnish the auditor general with information regarding its power, duties, activities, organization, financial transactions and methods of business as the auditor general requires, and the auditor general shall be given access to all books, accounts, financial records, reports, electronic data processing records, explanations, files and all other papers, things or property belonging to or in use by the department, agency of the Crown or Crown controlled corporation and necessary to the performance of the duties of the auditor general under this Act.

18. (1) The auditor general may examine a person on oath or affirmation on a matter pertinent to an account submitted to the auditor general for audit and the oath or affirmation may be administered by the auditor general to a person whom the auditor general desires to examine.

(2) In order to compel the attendance of a person under subsection (1), the auditor general may apply to a judge of the Trial Division for an order that a subpoena be issued from the court commanding the person named in the subpoena to appear before the auditor general at the time and place mentioned in the subpoena, and then and there to testify to all matters within that person's knowledge relative to an account submitted to the auditor general.

## Appendix I

(3) Where so required, the person named in the subpoena shall produce a document, paper or thing which he or she has possession of relative to the account.

(4) A person named in a subpoena issued under this section is entitled to reasonable expenses at the time of the service.

19. Notwithstanding sections 17 and 18, the auditor general shall not be permitted access to reports arising out of the conduct of lawful police investigations or to information in the records listed in paragraphs 9(1)(b) to (f) of *The Freedom of Information Act* except for the information in the records disclosed under subsection 9(2) of that Act.

20. The auditor general may station in the offices of a department, agency of the Crown or Crown controlled corporation, an employee of the office for the purpose of enabling the auditor general to more effectively exercise or perform his or her powers and duties under this or another Act, and the department, agency of the Crown or Crown controlled corporation shall provide the necessary office accommodation and facilities for employees so stationed.

21. The auditor general and each person employed in the office or appointed or engaged to assist the auditor general for a limited period of time or in respect of a particular matter under section 28 shall keep confidential all matters that come to his or her knowledge in the course of his or her employment or duties under this Act and shall not communicate those matters to another person, except as may be required in connection with the discharge of his or her responsibilities under this Act or under the *Criminal Code*.

22. Audit working papers of the office shall not be laid before the House of Assembly or a committee of the House of Assembly.

23. (1) Those auditors and employees that are necessary to enable the auditor general to perform his or her duties under this or another Act shall be appointed or employed in the manner authorized by law and are members of the public service of the province.

(2) The personnel management policies of the Treasury Board as they relate to the public service of the province apply to the office.

(3) *The Conflict of Interest Act, 1973* applies to the auditor general and every person employed in the office.

24. (1) Every person employed in the office, shall, before performing a duty as an employee in the office

(a) take or make and sign the Oath or Affirmation of Allegiance under *The Oaths of Office Act*; and

## Appendix I

- (b) take or make and sign the following oath or affirmation of office:

"I ....., do swear (or solemnly, sincerely and truly, declare and affirm) that I will faithfully, honestly and impartially to the best of my knowledge, skill and ability perform my duties as an employee in the Office of the Auditor General and that I will observe and comply with the laws of Canada and Newfoundland and except as I may be legally required, I will not disclose or give to a person information or a document that comes to my knowledge or possession by reason of my being an employee in the Office of the Auditor General." (In the case where an oath is taken add "So help me God").

(2) The oaths or affirmations referred to in subsection (1) shall be administered by the auditor general or his or her designate.

(3) The auditor general may require a person or class of persons appointed to assist the auditor general for a temporary period of time or in respect of a particular matter under section 28 to take or make and subscribe the oaths or affirmations referred to in subsection (1).

(4) A copy of each oath or affirmation administered to an employee of the office under subsection (1) shall be kept in the files of the office.

(5) The refusal of an employee of the office to take or make and subscribe to the oaths or affirmations or the failure to adhere to the oaths or affirmations required by subsection (1) may be considered as cause for dismissal.

25. (1) All persons employed in the office are employees for the purposes of the *Public Service Pensions Act, 1991* and are entitled to all the benefits under that Act.

(2) Notwithstanding subsection (1), the Lieutenant Governor in Council may by order permit the auditor general to participate in the *Public Service Pensions Act, 1991* or may by order stipulate other pension arrangements for the auditor general upon his or her appointment under this Act.

26. The auditor general may delegate in writing to an employee of the office authority to exercise a power or perform a duty of the auditor general other than reporting to the House of Assembly.

27. The auditor general may appoint an employee of the office as acting auditor general while the auditor general is absent from the province.

28. The auditor general may engage, on a fee basis, a person to act as his or her agent for the purpose of conducting an audit or examination that the auditor general is empowered to conduct or to perform a service that the auditor general considers necessary for a purpose related to the exercise or performance of the auditor general's powers and duties under this or another Act.

29. The auditor general, persons employed in the office and those persons employed or engaged by the auditor general under the authority of section 28 are not liable in a proceeding for an act done or not done or for a statement or report made by them in good faith in connection with a matter they are authorized or required to do under this Act.

## Appendix I

30. Subject to *The Public Tender Act, 1984*, the auditor general may engage within the limits of the appropriation approved by the Legislature for his or her office and without the approval of the Treasury Board the professional services, including counsel, consultants, accountants and other experts and acquire goods that the auditor general considers necessary for a purpose related to the exercise or performance of his or her powers and duties under this or another Act.

31. Where the auditor general

- (a) considers it necessary to report for the information of the Lieutenant-Governor in Council; or
- (b) is required to report to the Lieutenant-Governor in Council for the purposes of this Act, especially in respect of a matter relating to the office, the report is made through the Minister of Finance.

32. (1) The Commission shall appoint a qualified auditor to audit annually the office.

(2) The auditor appointed under subsection (1), has the same powers and shall perform the same duties in relation to an audit of the office that the auditor general has or performs in relation to an audit performed under this Act.

(3) The auditor appointed under subsection (1) shall submit his or her report to the commission and send a copy to the auditor general.

(4) The Speaker of the House of Assembly shall table the report of the auditor under this section before the House of Assembly immediately after receiving the report by him or her or where the House of Assembly is not then in Session, on the 1st day of the commencement of the next ensuing Session of the House of Assembly or the 1st day after the House of Assembly resumes sitting following an adjournment of the House of Assembly.

33. (1) The auditor general shall submit annually to the commission for its approval estimates of the sums that will be required to be provided by the Legislature for the payment of the salaries, allowances and expenses of the office under this Act during the next ensuing fiscal year.

(2) The commission shall review and may alter as it considers proper the estimates submitted under subsection (1) and, upon completion of the review, the Speaker of the House of Assembly shall submit the estimates as approved by the commission to the House of Assembly for the purpose of inclusion in the estimates of the province for approval by the Legislature.

34. (1) Where the auditor general conducts examinations or audits an agency of the Crown or Crown controlled corporation, the auditor general may charge fees for professional services rendered by his or her office.

(2) The fees referred to in subsection (1) shall be established on a basis that may be approved by the Lieutenant-Governor in Council.



## Appendix I

(3) The fees charged and collected by the auditor general under this section shall be paid into the Consolidated Revenue Fund.

35. (1) Persons in the employ of the Department of the Auditor General at the commencement of this Act are considered to have been appointed in accordance with this Act.

(2) Upon the commencement of this Act, the Department of the Auditor General is considered to be and is continued in the name of the Office of the Auditor General under this Act.

(3) A reference in another Act to the auditor general appointed under *The Financial Administration Act, 1973* or a reference in another Act to the auditor general shall be considered to be a reference to the auditor general appointed under this Act.

36. (1) Paragraph 2(a) of *The Financial Administration Act, 1973* is repealed and the following substituted:

“(a) “auditor general” means the Auditor General of Newfoundland appointed under the *Auditor General Act* and includes all employees acting under the auditor general's direction;”.

(2) Sections 58 to 71 of the Act are repealed.

(3) Subsection 83(1) of the Act is amended by striking out the words “and the Auditor General” and the words “or the Auditor General”.



## **Appendix II**

Departmental Audits Performed by the Office of the Auditor General

### **General Government Sector**

Consolidated Fund Services

Executive Council

Finance

Government Services and Lands

Legislature

Public Service Commission

Works, Services and Transportation

### **Resource Sector**

Development and Rural Renewal

Environment and Labour

Fisheries and Aquaculture

Forest Resources and Agrifoods

Industry, Trade and Technology

Mines and Energy

Tourism, Culture and Recreation

### **Social Sector**

Education

Health and Community Services

Human Resources and Employment

Justice

Municipal and Provincial Affairs

## Appendix III

| <u>Entity</u>                                              | <u>Year End</u>  | <u>Auditors<br/>Report</u> |
|------------------------------------------------------------|------------------|----------------------------|
| <b>Department of Development and Rural Renewal</b>         |                  |                            |
| Enterprise Network Inc.                                    | 31 March 1999    | Not completed              |
| Enterprise Newfoundland and Labrador                       | 31 March 1999    | Not completed              |
| Farm Development Loan Board                                | 31 March 1999    | Not completed              |
| Fisheries Loan Board of Newfoundland                       | 31 March 1999    | Not completed              |
| <b>Department of Education</b>                             |                  |                            |
| Newfoundland and Labrador Education Investment Corporation | 31 March 1999    | Not completed              |
| Provincial Information and Library Resources Board         | 31 March 1999    | 11 June 1999               |
| <b>Executive Council</b>                                   |                  |                            |
| Advisory Council on the Economy                            | 31 March 1999    | 31 May 1999                |
| Labrador Transportation Initiative Fund                    | 31 March 1999    | 19 May 1999                |
| Provincial Advisory Council on the Status of Women         | 31 March 1999    | 18 May 1999                |
| <b>Department of Finance</b>                               |                  |                            |
| Hotel Buildings Limited                                    | 31 March 1999    | 10 June 1999               |
| Marble Mountain Development Corporation                    | 30 April 1999    | 15 July 1999               |
| Newfoundland Government Fund Limited                       | 31 December 1998 | 15 April 1999              |
| Newfoundland Government Sinking Fund                       | 31 March 1999    | 18 June 1999               |
| Newfoundland Industrial Development Corporation            | 31 March 1999    | 16 June 1999               |
| Newfoundland Municipal Financing Corporation               | 31 March 1998    | 25 June 1998               |
| Province of Newfoundland Pooled Pension Fund               | 31 December 1998 | 8 March 1999               |
| <b>Department of Forest Resources and Agrifoods</b>        |                  |                            |
| Livestock Owners Compensation Board                        | 31 March 1999    | 15 June 1999               |
| Newfoundland Crop Insurance Agency                         | 31 March 1999    | 15 June 1999               |

## Appendix III

Agencies of the Crown and other Entities Whose Financial Statements Audits are Performed by the Office of the Auditor General

| <u>Entity</u>                                                      | <u>Year End</u>  | <u>Auditors Report</u> |
|--------------------------------------------------------------------|------------------|------------------------|
| <b>Department of Government Services and Lands</b>                 |                  |                        |
| Public Accountants' Licensing Board                                | 31 December 1998 | 15 June 1999           |
| <b>Department of Health and Community Services</b>                 |                  |                        |
| Newfoundland Medical Care Commission                               | 31 March 1999    | 25 June 1999           |
| <b>Department of Industry, Trade and Technology</b>                |                  |                        |
| Bull Arm Site Corporation                                          | 31 March 1999    | 8 June 1999            |
| <b>Department of Justice</b>                                       |                  |                        |
| Director of Support Enforcement                                    | 31 March 1999    | 4 June 1999            |
| Newfoundland Legal Aid Commission                                  | 31 March 1999    | Not completed          |
| Office of the High Sheriff                                         | 31 March 1999    | Not completed          |
| Registrar of the Supreme Court of Newfoundland                     | 31 March 1999    | 8 July 1999            |
| <b>Department of Municipal and Provincial Affairs</b>              |                  |                        |
| Newfoundland and Labrador Housing Corporation                      | 31 March 1999    | 28 June 1999           |
| <b>Department of Tourism, Culture and Recreation</b>               |                  |                        |
| Heritage Foundation of Newfoundland and Labrador                   | 31 March 1999    | 8 June 1999            |
| Newfoundland and Labrador Arts Council                             | 31 March 1999    | 25 June 1999           |
| Special Celebrations Corporation of Newfoundland and Labrador Inc. | 31 March 1999    | 17 June 1999           |
| <b>Department of Works, Services and Transportation</b>            |                  |                        |
| C.A. Pippy Park Commission                                         | 31 March 1999    | 18 June 1999           |

## Appendix IV

Agencies of the Crown and Other Entities Whose Financial Statements Audits are Performed by Private Sector Auditors

| <u>Entity</u>                                                           | <u>Year End</u>  | <u>Auditors<br/>Report</u> |
|-------------------------------------------------------------------------|------------------|----------------------------|
| <b>Department of Development and Rural Renewal</b>                      |                  |                            |
| Newfoundland and Labrador Film Development Corporation                  | 31 March 1999    | 14 July 1999               |
| <b>Department of Education</b>                                          |                  |                            |
| Memorial University of Newfoundland                                     | 31 March 1999    | 21 May 1999                |
| Memorial University of Newfoundland Pension Plan                        | 31 March 1999    | 21 May 1999                |
| The College of the North Atlantic                                       | 31 March 1999    | 17 June 1999               |
| Literacy Development Council of Newfoundland and Labrador               | 31 March 1999    | 27 July 1999               |
| <b>School Boards</b>                                                    |                  |                            |
| District #1 - Labrador                                                  | 30 June 1998     | 31 July 1998               |
| District #2 - Northern Peninsula/Labrador South                         | 30 June 1998     | 2 September 1998           |
| District #3 - Corner Brook/Deer Lake/St. Barbe                          | 30 June 1998     | 4 September 1998           |
| District #4 - Cormack Trail                                             | 30 June 1998     | 24 September 1998          |
| District #5 - Baie Verte/Central/Connaigre                              | 30 June 1998     | 18 September 1998          |
| District #6 - Lewisporte/Gander                                         | 30 June 1998     | 10 October 1998            |
| District #7 - Burin                                                     | 30 June 1998     | 11 December 1998           |
| District #8 - Vista                                                     | 30 June 1998     | 28 October 1998            |
| District #9 - Avalon West                                               | 30 June 1998     | 17 November 1998           |
| District #10 - Avalon East                                              | 30 June 1998     | 16 March 1999              |
| Conseil Scolaire Francophone Provincial de Terre - Neuve et du Labrador | 30 June 1998     | Not received               |
| <b>Department of Environment and Labour</b>                             |                  |                            |
| Multi-Materials Stewardship Board                                       | 31 March 1999    | Not received               |
| Workplace Health, Safety and Compensation Commission                    | 31 December 1998 | 15 March 1999              |

## Appendix IV

A summary of the financial and other entities whose financial statement audits are performed by the Auditor General of Newfoundland.

| <u>Entity</u>                                           | <u>Year End</u>  | <u>Auditors Report</u> |
|---------------------------------------------------------|------------------|------------------------|
| <b>Department of Finance</b>                            |                  |                        |
| Marble Mountain Management Corporation                  | 30 April 1999    | 30 June 1999           |
| Newfoundland Liquor Corporation                         | 31 March 1999    | Not received           |
| <b>Department of Forest Resources and Agrifoods</b>     |                  |                        |
| Newfoundland Farm Products Corporation                  | 31 March 1999    | 3 September 1999       |
| <b>Department of Government Services and Lands</b>      |                  |                        |
| Credit Union Deposit Guarantee Corporation              | 31 December 1998 | 9 March 1999           |
| Board of Commissioners of Public Utilities              | 31 March 1999    | 7 May 1999             |
| <b>Department of Health and Community Services</b>      |                  |                        |
| Newfoundland Cancer Treatment and Research Foundation   | 31 March 1999    | 21 May 1999            |
| Provincial Genetics Program                             | 31 March 1999    | 23 June 1999           |
| Provincial Perinatal Program                            | 31 March 1999    | 23 June 1999           |
| Public Health Laboratory                                | 31 March 1999    | 23 June 1999           |
| Newfoundland and Labrador Centre for Health Information | 31 March 1999    | 21 July 1999           |
| <b>Community Health Boards</b>                          |                  |                        |
| Central Regional Health and Community Services Board    | 31 March 1999    | 23 June 1999           |
| Eastern Regional Health and Community Services Board    | 31 March 1999    | 4 June 1999            |
| St. John's Regional Health and Community Services Board | 31 March 1999    | 16 June 1999           |
| Western Regional Health and Community Services Board    | 31 March 1999    | 9 June 1999            |

## Appendix IV

Appendix IV of the Financial and Other Entities Whose Financial Statements Audits are Performed by the Auditor General

| <u>Entity</u>                                                | <u>Year End</u>  | <u>Auditors Report</u> |
|--------------------------------------------------------------|------------------|------------------------|
| <b>Department of Health (cont'd)</b>                         |                  |                        |
| <b>Regional Hospital Boards</b>                              |                  |                        |
| Avalon Health Care Institutions Board                        | 31 March 1999    | 30 July 1999           |
| Central East Health Care Institutions Board                  | 31 March 1999    | 11 August 1999         |
| Central West Health Corporation                              | 31 March 1999    | 28 July 1999           |
| Grenfell Regional Health Services Board                      | 31 March 1999    | Not received           |
| Health Care Corporation of St. John's                        | 31 March 1999    | 23 June 1999           |
| Health Labrador Corporation                                  | 31 March 1999    | Not received           |
| Peninsulas Health Care Corporation                           | 31 March 1999    | 26 July 1999           |
| Western Health Care Corporation                              | 31 March 1999    | 18 June 1999           |
| <b>Nursing Homes</b>                                         |                  |                        |
| Pentecostal Assemblies - Clarke's Beach Senior Citizens Home | 31 March 1999    | 16 June 1999           |
| St. John's Nursing Home Board                                | 31 March 1999    | Not received           |
| <b>Department of Industry, Trade and Technology</b>          |                  |                        |
| Newfoundland Hardwoods Limited                               | 31 March 1999    | 9 June 1999            |
| Newfoundland Ocean Enterprises Limited                       | 31 March 1999    | 7 July 1999            |
| Operation ONLINE Inc.                                        | 31 March 1999    | 10 June 1999           |
| <b>Department of Mines and Energy</b>                        |                  |                        |
| Churchill Falls (Labrador) Corporation Limited               | 31 December 1998 | 29 January 1999        |
| Gull Island Power Company Limited                            | 31 December 1998 | 29 January 1999        |
| Lower Churchill Development Corporation Limited              | 31 December 1998 | 29 January 1999        |
| Newfoundland and Labrador Hydro Electric Corporation         | 31 December 1998 | 16 February 1999       |
| Twin Falls Power Corporation Limited                         | 31 December 1998 | 29 January 1999        |



## Appendix IV

Statements of the Auditor General and Other Officials of the Government of Newfoundland and Labrador are published in the Auditor General's Report.

| <u>Entity</u>                                         | <u>Year End</u> | <u>Auditors<br/>Report</u> |
|-------------------------------------------------------|-----------------|----------------------------|
| <b>Department of Municipal and Provincial Affairs</b> |                 |                            |
| Municipal Assessment Agency Inc.                      | 31 March 1999   | 12 May 1999                |
| <b>Department of Tourism, Culture and Recreation</b>  |                 |                            |
| The John Cabot (1997) 500th Anniversary Corporation   | 31 March 1999   | 14 September 1999          |